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March 2, 2015

VIA HAND DELIVERY

Honorable Mayor and Members of the City Council
City of Fremont
3300 Capitol Avenue
Fremont, CA 94538

Re: Amendments to Affordable Housing Ordinance
(Fremont Municipal Code Chapter 18.155)
City Council Meeting of March 3, 2015

Dear Honorable Mayor and Members of the City Council:

This letter is submitted on behalf of the Building Industry Association of the Bay Area. It concerns the proposed amendments to the City's Affordable Housing Ordinance on the City Council's March 3, 2015 agenda, including adoption of new or revised affordable housing fees to mitigate impacts allegedly created by market-rate housing (including for-sale and rental housing) on the need for affordable housing within the City of Fremont.

The fees are based upon a "Residential Nexus Analysis" prepared by Keyser Marston Associates (KMA), dated August 2014. The KMA nexus study claims to justify affordable housing fees ranging from $26.40 per square foot for single-family homes to $32.70 per square foot for apartments. It relies on the proposition that affordable housing needs are attributable to new market-rate housing, which it purports to demonstrate by use of two models that rely on a series of assumptions about the economic and social effects of construction of a new market-rate home in Fremont. The methodology employed by KMA has not been empirically validated, is not reasonably established in the expert literature, bears no resemblance to the standard methodologies used to demonstrate impacts from development, and conflates causation and correlation. It makes no attempt to test its conclusions against the substantial body of governmental and academic literature and supporting data identifying the root causes of affordable housing needs. These data, studies and reports show that the lack of affordable housing is the result of a complex amalgam of factors, including restrictive zoning and growth controls, excessive impact fees, complex environmental regulations, high land prices, multifamily housing restrictions, and NIMBYism.

We respectfully submit that the KMA nexus study does not furnish an adequate evidentiary or analytic basis for the conclusion that a reasonable relationship exists between the proposed fees and the impact of new residential development, and that approval of the proposed fees in reliance on the nexus study would not conform to the requirements of law.

I. INTRODUCTION AND EXECUTIVE SUMMARY

A. The KMA Residential Nexus Analysis.

The KMA study purports to both "document[] and quantif[y] the linkages between new market-rate residential development in the City of Fremont and the demand for additional affordable housing." (Nexus Study at 9). The nexus study describes the methodology employed in the analysis as follows:

> At its most simplified level, the underlying nexus concept is that the newly constructed units represent net new households in Fremont. These households represent new income in Fremont that will consume goods and services, either through purchases of goods and services or "consumption" of governmental services. New consumption translates to jobs; a portion of the jobs are at lower compensation levels; low compensation jobs relate to lower income households that cannot afford market rate units in Fremont and therefore need affordable housing.

Id. at 9.

The methodology begins with five "prototypical market-rate units" (four for-sale and one rental); assumes a purchase price or rental rate for those units; estimates the gross household income of the people buying or renting the units; estimates the net household income available for expenditures; assumes a rate of expenditure on local goods and services within Alameda County; uses an IMPLAN model to estimate (i) the number of jobs generated in Alameda County "at establishments that serve new residents directly;" (ii) the jobs generated "by increased demand at firms which service or supply these establishments;" and (iii) the jobs generated when the new employees in the jobs described in (i) and (ii) "spend their wages in the local economy;" uses a separate KMA "jobs housing nexus analysis model" to translate these jobs into new households; estimates the size and occupational and income distribution of the households; estimates the number of these households that fall within inclusionary housing parameters; calculates the total development cost of new market-rate units that would accommodate those households; deducts the amounts necessary to make those units affordable to the various tiers of new low- or moderate-income households; and thereby purports to calculate the "affordability gap" for each of these tiers of households "generated" by new market-rate units. This "affordability gap" is then translated into the "total nexus cost" for each new market-rate unit.

This multi-step causation analysis, in turn, rests upon a host of assumptions about matters such as household income of occupants of market-rate units, tax, personal savings and debt rates, local

(versus regional or online) spending patterns, number, type and location of net new jobs created, number of persons from outside the community occupying those jobs, size, number and total income of new households "created" by those jobs, and other variables.

B. Governing Law.

Affordable housing fees, like other development impact exactions, "must bear a reasonable relationship, in both intended use and amount, to the deleterious public impact of the development." *San Remo Hotel v. City and County of San Francisco,* 27 Cal.4th 643, 663–664 (2002). Under the Mitigation Fee Act, Govt. Code, §§ 66000–66025, the local agency must demonstrate a "reasonable relationship" between the need for and use of the exaction and the type of development project on which the exaction is imposed. Govt. Code § 66001(a)(3). The local agency bears the burden of producing evidence in support of these determinations. *Homebuilders Ass'n of Tulare/Kings Counties, Inc. v. City of Lemoore*, 185 Cal.App.4th 554, 561 (2010). The agency must also show that a valid method was used for establishing a reasonable relationship between the fee charged and the impact of the development. *Shapell Industries, Inc. v. Governing Board*, 1 Cal.App.4th 218, 235 (1998).

The Mitigation Fee Act embodies both constitutional and statutory standards. *Ehrlich v. City of Culver City*, 12 Cal. 4th 854, 866–67 (1996) (Term "reasonable relationship" as used in Mitigation Fee Act "embraces both constitutional and statutory meanings" and should be construed in light of both federal and state constitutional jurisprudence); *accord*, *San Remo Hotel v. City and County of San Francisco*, 27 Cal. 4th 643, 663–664 (2002) ("As a matter of both statutory and constitutional law, [exactions] must bear a reasonable relationship, in both intended use and amount, to the deleterious public impact of the development."). This standard reflects fundamental fairness principles under federal and state takings law, which prevent the government from "forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." *United States v. Armstrong*, 364 U.S. 40, 49 (1960); *accord, Palazzolo v. Rhode Island*, 533 U.S. 606, 617–618 (2001); *Lockaway Storage v. County of Alameda*, 216 Cal. App. 4th 161, 183 (2013). California courts have explicitly recognized that this fairness principle is central to takings law both in the context of regulatory takings and in the realm of inverse condemnation resulting from other governmental acts or omissions that damage or destroy property. *See, e.g.*, *Holtz v. Superior Court*, 3 Cal. 3d 296, 303–304 (1970); *Liberty v. California Coastal Commission*, 113 Cal. App. 3d 491, 504 (1980).

In *Shapell,* 1 Cal. App. 4th at 2357, the court explained that "[w]hile it is 'only fair' that the public at large should not be obliged to pay for the increased burden on public facilities caused by new development, the converse is equally reasonable: the developer must not be required to shoulder the entire burden of financing public facilities for all future users." Under this principle, "[i]t follows that [impact] fees are justified only to the extent that they are limited to the cost of

increased services made necessary by virtue of the development." *Id.* at 236. The local agency must therefore show that "a *valid method* was used for arriving at the fee in question, 'one which established a reasonable relationship between the fee charged and the burden posed by the development.'" *Id.*, quoting *Bixel Associates v. City of Los Angeles,* 216 Cal.App.3d 1208, 1219 (1989) (emphasis added).

The mandate that the fee be "reasonably related," according to its plain meaning, requires a reasonable causal connection between the development and the impact sought to be addressed. *San Remo Hotel v. City and County of San Francisco,* 27 Cal. 4th 643, 687 (2002) ("[F]ee does not violate the Takings Clause so long as (1) there is a cause-and-effect relationship between the owner's desired use of the property and the social evil that the fee seeks to remedy, and (2) the fee is reasonably related in both intended use and amount to that social evil." (Baxter, J. concurring and dissenting); *Homebuilders Ass'n of Tulare/Kings Counties, Inc. v. City of Lemoore,* 185 Cal.App.4th 554, 576 (2010) (Ardaiz, J. concurring) (close connection required).

If no reasonable causal connection exists between new residential development and affordable housing needs, the agency cannot sustain the burden under the Mitigation Fee Act of establishing that there is a reasonable relationship between (1) the development and the *need* for affordable housing; (2) the development and the *use* of the exaction to provide affordable housing; or (3) the amount or extent of the exaction and the *cost* of the affordable housing attributable to the development. Govt. Code §§ 66001(a)(3)–(4);(b). Without that relationship, the affordable housing fee also constitutes an unconstitutional condition because the government is effectively requiring the applicant to give up constitutional rights under the Takings Clause[1] in order to obtain the required permits. *Koontz v. St. Johns River Water Management District*, 133 S. Ct. 2586, 2596 (2013) (Demands for money or property in the land-use permitting context lacking the required nexus with the presumed impact "run afoul of the Takings Clause not because they take property but because they impermissibly burden the right not to have property taken without just compensation.")

Proximate cause analysis -- which is routinely used by courts in a variety of contexts including cases arising under the Takings Clause -- informs the determination whether the causal component of the reasonable-relationship standard is satisfied. *See Penn. Cent. Transp. Co. v. New York City*, 438 U.S. 104, 124 (1978) ("[W]hether a particular restriction will be rendered invalid by the government's failure to pay for any losses proximately caused by it depends largely upon the particular circumstances in that case."); *Belair v. Riverside County Flood Control Dist.*, 47 Cal. 3d 559 (1988). This analysis asks both whether a sufficient causal

[1] Unless otherwise indicated, references to the "Takings Clause" are to the corresponding clauses of the federal and state constitutions, which the California Supreme Court has interpreted congruently in the context of regulatory takings. *See San Remo Hotel*, 27 Cal. 4th at 667.

connection exists in fact and whether fairness and justice warrant requiring the property owner, rather than society as a whole, to address the social impact through mitigation. Proximate causation reflects both "'ideas of what justice demands'" and "'of what is administratively possible and convenient,'" *Anza Steel v. Ideal Steel Supply Corp.*, 547 U.S. 451 (2006). California courts have highlighted the close connection between the proximate cause requirement and the constitutional fairness doctrine (referred to in the inverse condemnation context as the "loss distribution premise"). *See Holtz v. Superior Court*, 3 Cal. 3d 296, 303–304 (1970). The proximate cause inquiry works to answer the same question as the reasonable-relationship test—whether the development is sufficiently connected with the targeted social problem to make it fair and reasonable to require the property owner to address it through mitigation.

C. Application.

An expert study or report can be a valuable aid in demonstrating the necessary causal link (in nature and extent) between new development and societal impacts (as exemplified by engineering studies routinely employed to establish appropriate mitigation for impacts on traffic, storm drainage and wastewater, or by analyses matching student enrollment with new homes to establish actual student generation rates and calculate school impact fees). However, in order for such expert opinion or analysis to be validly relied upon, it must have some grounding in the facts and must reflect accepted principles and methods. The reasonable-relationship determination required by law cannot be satisfied simply by an expert's assurance -- without any empirical support or generally accepted methodology -- that the required factual connection exists. Courts have long held that an expert's opinion must be based upon assumptions considered reasonable by experts in the same field and "is no better than the facts on which it is based." *Kennemur v. State of California,* 133 Cal. App. 3d 907, 923 (1982). "Where an expert bases his conclusion upon assumptions . . . which are not reasonably relied upon by other experts, or upon factors which are speculative, remote or conjectural, then his conclusion has no evidentiary value . . . ." *Pacific Gas & Electric Co. v. Zuckerman*, 189 Cal.App.3d 1113, 1135 (1987); *City of San Diego v. Sobke*, 65 Cal.App.4th 379, 396 (1998).

As with a court, an agency can and should disregard expert opinion that lacks an adequate factual foundation or is not based upon a generally accepted methodology. For example, "an expert's opinion which says nothing more than 'it is reasonable to assume' that something 'potentially ... may occur'" but has no basis in fact and does not constitute substantial evidence that can reasonably be relied on by a public agency. *See Apartment Association of Greater Los Angeles v. City of Los Angeles*, 90 Cal.App.4th 1162, 1173-1176 (2001). *See also Lucas Valley Homeowners Ass'n v County of Marin,* 233 Cal. App. 3d 130 (1991) (Expert testimony by real estate agent regarding potential decline in property values was not substantial evidence because it was an imprecise opinion without supporting verifiable data such as comparables); *Citizens*

Comm. to Save Our Village v City of Claremont, 37 Cal. App. 4th 1157, 1170 (1995) (no factual foundation for architect's letter claiming a historically significant landscape plan had been implemented on project site); *Gentry v City of Murrieta,* 36 Cal. App. 4th 1359, 1422 (1995) (letter from engineering professor about groundwater and erosion impacts was not substantial evidence because it was not based on an adequate factual foundation).

The KMA Nexus Study, with its lengthy series of unverified assumptions, neither establishes the required causal connection between new development and affordable housing needs nor shows why it is fair and reasonable to require development applicants – rather than the general public – to shoulder the burden of providing affordable housing. It does not establish that new residential development "causes" or even contributes to the need for affordable housing. It merely shows that if a lengthy series of assumptions – some secondary, tertiary and beyond – about economic and social dynamics is embedded into two models, the impact of a new market rate unit on affordable housing needs can be demonstrated with precision. It offers no empirical support for many of these assumptions or for its counterintuitive conclusions. The lack of affordable housing has been a problem in California for decades. Scores of government and academic studies, supported by a wealth of research and economic data, have demonstrated that the need for affordable housing has been generated over an extended period by a complex amalgam of factors, including restrictive zoning and growth controls, impact fees, complex environmental regulations, high land prices, multifamily housing restrictions, and NIMBYism. None of these studies has shown or even posited any causal relationship between new residential development and affordable housing needs.

The nexus study, on the other hand, is not based on any research or empirical evidence supporting a cause-and-effect relationship between new market-rate housing and the need for affordable housing. It does not assess, rely on, attempt to controvert or even mention the substantial body of governmental and academic literature and supporting data identifying the root causes of affordable housing needs. Nor is the nexus study itself based upon any body of established academic, scientific or technical literature. A comprehensive review of potentially relevant sources in 2011 (including journal articles, books, presentations and government reports) failed to disclose any literature -- peer-reviewed or otherwise -- supporting the methodology used in the residential nexus analyses.[2] The nexus study (together with its 2010 predecessor) was developed specifically for the purpose of supporting affordable housing impact fees on new residential development in the wake of *Palmer* and *Patterson.* Thus, in addition to lacking any empirical justification and failing to controvert the large body of academic, technical

[2] Cray, A., *The Use of Residential Nexus Analysis in Support of California's Inclusionary Housing Ordinances: A Critical Evaluation: A report to the California Homebuilding foundation* (Nov. 2011) at 7 (available at http://www.cbia.org/go/linkservid/06D3172D-35C3-4C71-9A9098D439C63874/showMeta/0/).

and governmental literature identifying other causes of affordable housing needs, the nexus study employs a methodology that has not been generally accepted, or even considered, by the academic, scientific or technical community. It relies entirely on a combination of hypotheses and modeling to construct a theory under which a market-rate home generates economic forces that create a "need" for a below-market-rate home. But it fails to demonstrate that the new housing has any *causative*, as opposed to correlative, relationship with the need for affordable housing.

The nexus study's theoretical link between residential development and affordable housing needs falls far short of the *substantial* cause-and-effect relationship required under the reasonable-relationship standard and proximate cause principles. Causal chains far less tenuous have been rejected under proximate cause analysis simply because there are too many dependent assumptions and variables. The multitude of steps in the analysis, any one of which can be heavily skewed in one direction or another by independent factors, render the ultimate conclusion little more than speculation, which is antithetical to the "substantial cause-and-effect" relationship required by law.

The causation theory underlying the residential nexus analyses also fails the normative/evaluative component of proximate cause since it does not comport with the governing constitutional and statutory principles. The policies of reasonableness, fairness and justice embodied in the state and federal constitutions are not satisfied by studies that demonstrate only an attenuated and theoretical link between the development and the need.

The lack of affordable housing in California is a longstanding problem that exists for a multitude of reasons unrelated to new residential development. The costs of addressing it should, in fairness, be borne by society as a whole, not allocated to residential developers based on administrative convenience or leverage, or because government officials (and the electorate) have not made funding affordable housing a sufficient public policy priority.

III. BACKGROUND

A. Affordable Housing Needs in California.

The lack of affordable housing in California has been a major social and political issue since the 1970s. In 1975, the California legislature found that:

> there exists within the urban and rural areas of the state a serious shortage of decent, safe, and sanitary housing which persons and families of low or moderate income, including the elderly and handicapped, can afford. This situation creates an absolute present

> and future shortage of supply in relation to demand, as expressed in terms of housing needs and aspirations, and also creates inflation in the cost of housing, by reason of its scarcity, which tends to decrease the relative affordability of the state's housing supply for all its residents.[3]

The problem has steadily grown worse since. Thirteen of the fifteen least affordable metropolitan housing markets in the nation are in California.[4] The severity and intractability of the problem is exemplified by the dozens of legislative enactments designed to streamline the approval process and provide incentives to local agencies to approve affordable housing projects. *See, e.g.,* Housing Element Statutes (Gov't Code §§65580-65589.8 and §§65751-65761); Housing Accountability Act (§§65589.5-65589.6); prohibitions against discrimination against affordable housing (Id., §65008); statute of limitations (§65009); regional transportation plans (Id., § 65080 – 65086.5); "no net loss statute" (Id., §65863); "least cost" zoning law (Id., §§65913-65913.2); density bonus law (Id., §§65915-65918).

The legislature has found that:

> 1. The availability of housing is of vital statewide importance, and the early attainment of decent housing and a suitable living environment for every Californian, including farmworkers, is a priority of the highest order.
>
> 2. The early attainment of this goal requires the cooperative participation of government and the private sector in an effort to expand housing opportunities and accommodate the housing needs of Californians of all economic levels.

And, of particular importance to the questions presented here, the Legislature has also found that:

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[3] Gov't Code section 50003(a).

[4] Wells Fargo/NAHB Housing Opportunity Index; 4th Quarter 2014 (available at http://www.nahb.org/reference_list.aspx?sectionID=132). Several reports have concluded that the state is now adding approximately three jobs for every housing unit constructed. Fulton, William, "Housing Rises on Sacramento's List of Priorities," California Planning and Development Report (Solimar Research Group 2000) (available at http://www.cp-dr.com/node/1373).

> California housing has become the most expensive in the nation. The excessive cost of the state's housing supply is partially caused by activities and policies of many local governments that limit the approval of housing, increase the cost of land for housing, *and require that high fees and exactions be paid by producers of housing.* (*Id.*, §65589.5, emphasis added)

Scores of studies; reports and planning documents have demonstrated that the lack of affordable housing is the result of a complex interaction of factors, including California's chronic undersupply of new housing units generally relative to job and population growth, restrictive zoning and growth controls, excessive impact fees, complex environmental regulations, obsolete building codes, multifamily housing restrictions, high land prices and NIMBYism.[5] Indeed, the term "inclusionary zoning" was coined in deliberate contrast to "exclusionary zoning," and some affordable housing advocates have justified inclusionary housing policies as "a means to recapture land prices that have been artificially inflated by communities' exclusionary policies."[6] New residential development is not among the factors cited in any of these studies as creating a need for affordable housing. Even ardent defenders of the legality of these nexus studies, in moments of candor, recognize as much:

> Has the need for affordable housing increased in recent years? Yes, it has.... The need has increased recently, particularly in parts of the State such as the San Francisco Bay Area, due to a confluence of several factors. First, the demise of redevelopment and a reduction in federal programs have led to a serious drop in funding available to affordable housing. For example, in Santa Clara County, it has been estimated that total funding available for affordable housing in 2008 (the last 'normal' year) was approximately $126 million. In 2013, the corresponding number was $47 million.... The second factor has been the booming local economy. That has lowered the vacancy rate on rental housing, created a

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[5] *See "Why Not In Our Community?" Removing Barriers to Affordable Housing. An Update to the Report of the Advisory Commission on Regulatory Barriers to Affordable Housing* (HUD 2004) at 5 (available at http://www.huduser.org/portal/Publications/wnioc.pdf); City of Fremont 2015-2022 General Plan Housing Element at 23; *see also id.* at 151: *America's Rental Housing: Evolving Markets and Needs* (Joint Center for Housing Studies – Harvard Univ., Dec. 2013) (available at http://www.jchs.harvard.edu/americas-rental-housing)

[6] Kautz, B., *Comment, In Defense of Inclusionary Zoning: Successfully Creating Affordable Housing*, 36 U.S.F. L. Rev. 971, 983 (2002).

> white-hot real estate market for medium- to high-density multi-family housing, but of course, also raised rents.[7]

While no single factor is identified in these studies as the sole or principal cause of affordable housing issues, a unifying theme of these studies is that affordable housing needs are a broad social problem that must be addressed through a comprehensive range of policy responses and measures (including streamlining the development approval process, eliminating restrictive zoning regulations, providing financial incentives, counteracting NIMBYism, reducing the complexity and uncertainty of environmental requirements). The societal dimension of the problem is reflected in the California Legislature's passage of "no less than 19 different sets of laws and programs [in] efforts to both increase the housing available to Californians and to help make it affordable.") *See Wilson v. City of Laguna Beach*, 6 Cal. App. 4th 543, 545 (1992).[8]

Yet state and local governments have not accorded affordable housing anything close to the fiscal resources necessary to meaningfully address the problem.[9] Although surveys have shown a willingness of the public to devote more resources toward addressing the problem,[10] *fewer,* not

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[7] Faber, A., *Inclusionary Housing Requirements: Still Possible?* (September, 2014, presented at the League of California Cities City Attorneys' Department 2014 Annual Conference) at 2-3 (available at http://www.cacities.org/Resources-Documents/Member-Engagement/Professional-Departments/City-Attorneys/Library/2014/2014-Annual/9-2015-Annual-Andrew-Faber-Inclusionary-Housing-Re.aspx)

[8] The longstanding nature of the societal contract to meet the housing needs of all members of society is also spelled out in various federal measures, typical of which is the Housing Act of 1949 (42 USC §§ 1441–1490r), which calls for the "realization as soon as feasible of the goal of a decent home and suitable living environment for every American family."

[9] *See, e.g.,* Baldassare, M. and Hoene, C., *Local Budgets and Tax Policy in California: Surveys of City Officials* (Pub. Policy Inst. of Calif., Sept. 2004) (available at http://www.ppic.org/content/pubs/op/OP_904MBOP.pdf); Local Revenue Measures in California – June 2012 - November 2014 Results (California City Finance, Dec. 2014) (see Attachment A); An Overview of Local Revenue Measures in California Since 2001(California City Finance, March 2014) (available at http://www.californiacityfinance.com/LocalMeasuresSince01.pdf).

[10] *See, e.g.,* City of Mountain View Memorandum – Affordable Housing Voter Survey Results (March 1, 2012) (available at http://laserfiche.mountainview.gov/WebLink/0/doc/59402/Page5.aspx)

more public resources are going toward these needs as funds are being diverted to schools and other uses deemed higher priorities.[11] Increasingly, public agencies are turning to new market-rate housing to address these needs, heedless of the impact of this substantial additional burden on housing prices generally.[12] As the data indicate, the result of these costs piled on top of other regulatory burdens is fewer homes affordable to Californians, not more.[13]

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[11] *See* Financing California's Infrastructure (Sacramento State Univ., Dec. 2005) (available at http://www.csus.edu/calst/government_affairs/reports/financing_california.pdf); Strategic Growth Plan Bond Accountability (HCD 2007) (available at http://www.bondaccountability.hcd.ca.gov/); Proposition 1A (2004) Facts (California City Finance, Dec. 2007) (available at http://www.californiacityfinance.com/Prop1A_FAQ.pdf California Struggles with $1.7 Billion Loss in Redevelopment Funding (Multi-Housing News, Aug. 2013) (available at http://www.multihousingnews.com/features/california-struggles-with-1-7-billion-loss-in-redevelopment-funding/1004059743.html); Bount, C., et al., Redevelopment Agencies in California: History, Benefits, Excesses, and Closure (Social Science Electronic Publishing, June 2012 (available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2445536); Fulton, W., *Housing Rises on Sacramento's List of Priorities*, California Planning and Development Report, (Solimar Research Group 2000) (available at http://www.cp-dr.com/node/1373).

[12] The Governor recognized this impact in vetoing a bill designed to supersede the holding of *Palmer*. Veto Message: AB 1229 -- Governor Jerry Brown (available at http://gov.ca.gov/docs/AB_1229_2013_Veto_Message.pdf).

[13] *See. e.g.*, HCD -- Housing and Community Development 2014 Update, Highlights of the State Housing in California: Affordability Worsens, Supply Problems Remain (available at http://www.hcd.ca.gov/hpd/shp/web_hcd_stateofhousing_april2014.pdf); California Policy Center -- Housing Starts Authorized by Building Permits; 1 Unit Structures, California vs. Houston, 2011-2014 (May 2014) (available at http://californiapolicycenter.org/california-vs-texas-in-one-chart/); Myers, D., *The Great Housing Collapse in California*, (FannieMae Foundation, May 2002) (available at http://content.knowledgeplex.org/kp2/kp/text_document_summary/article/relfiles/fmf_0426_myers_park.pdf;) Five Truths of Tech-Hub Housing Costs (Trulia Trends, Feb. 2014) (available at http://www.trulia.com/trends/2014/02/price-and-rent-monitors-jan-2014/); California Building Industry Association – Housing Starts 1954-2013 (available at http://www.cbia.org/tasks/sites/cbia/assets/File/Historical%20Housing%20Starts%201954-2013.pdf).

B. The *Palmer* and *Patterson* Decisions.

The legal landscape concerning inclusionary housing requirements changed significantly in 2009 with the decisions in *Building Industry Association of Central California v. City of Patterson*, 171 Cal. App. 4th 886 (2009) and *Palmer/Sixth Street Properties L.P. v. City of Los Angeles*, 175 Cal. App. 4th 1396 (2009).

In *Patterson,* a homebuilder challenged an increase in an in-lieu fee adopted as part of an inclusionary housing ordinance. Relying on the California Supreme Court decision in *San Remo Hotel v. City and County of San Francisco*, 27 Cal. 4th 643, 663–664 (2002), the court found that the ordinance in question could only be upheld if it had a reasonable relationship to the "deleterious public impact of the development." *Patterson*, 171 Cal. App. 4th at 897–98. After careful evaluation of the evidence relied on by the City, the court concluded that the City had failed to show that its affordable housing in-lieu fee was reasonably related to the impact either of the plaintiff's development specifically or of new residential development generally. 171 Cal. App. 4th at 899.

In *Palmer,* the appellate court held that the City's requirement that developers of new rental housing set aside and rent a percentage of the units at rates affordable to lower-income households conflicted with the Costa Hawkins Act (Civil Code §§ 1954.50 *et seq.*). The Costa Hawkins Act permits developers to set the initial rents for both newly constructed and voluntarily vacated units. The court found that obligating the building owner to provide affordable housing at regulated rents was "clearly hostile" to the right under Costa-Hawkins to establish the initial rental rate for the apartment units. The court also concluded that the option of paying an in-lieu fee did not save the inclusionary requirement because payment of the fee was "inextricably intertwined" with the mandate to impose rent restrictions.

C. Post *Palmer* and *Patterson* Developments.

In order to avoid running afoul of the Costa Hawkins Act, as applied in *Palmer*, many municipalities, including Fremont, adopted "affordable housing impact fees" for rental housing. In contrast to the in-lieu fees invalidated in *Palmer* as "inextricably intertwined" with the rent ceilings, these fees are expressly characterized as impact fees intended to mitigate "the impact of new market rate housing development on the demand for affordable housing."[14]

[14] Keyser Marston Associates, Inc. Residential Nexus Analysis – City of Fremont (August 2014) at 1 ("KMA -- Fremont); Keyser Marston Associates, Inc. Residential Nexus Analysis – City of San José (June 2014) at 1 (available at http://www.sanJoséca.gov/DocumentCenter/View/32877) ("KMA--San José); *see also* RSG, *Nexus Study & Fee Analysis Summary – City of San Carlos*

At the same time, in implicit recognition of the difficulties in establishing a legally sustainable connection between new residential development and the need for affordable housing, the same municipalities continued to characterize (or recharacterize) their inclusionary housing requirements as something other than development exactions. On the advice of counsel[15] or at the urging of affordable housing advocates,[16] they continued to maintain, after *Palmer* and

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(Feb. 2, 2010) , Appendix 1:2 ("To comply with *Palmer/Sixth Street Properties v. City of Los Angeles*, the revised BMR Ordinance requires developers of rental housing to pay an affordable housing impact fee and does not require the provision of affordable rental housing.") (available at: http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=2&cad=rja&uact=8&ved=0CCQQFjAB&url=http%3A%2F%2Fwww.21elements.com%2FDownload-document%2F492-San-Carlos-Nexus-Study-Fee-Analysis.html&ei=GrXeU-7YFsekigLt0oGQDw&usg=AFQjCNENQomLUKYgifm2iRfUwAMbL8Q6jw&bvm=bv.72197243,d.cGE)

[15] *See, e.g.,* Faber, *supra*, at 8 ("While the author of this paper is optimistic that this rationale [that affordable housing requirements are justified under the police power] will be accepted by the Court, any city attorney giving conservative advice to his or her city would probably suggest doing a nexus study to justify the ordinance.")

[16] *See* Kautz, B., *Life After Palmer: What's Next? Local Responses to Palmer and Patterson.* Paper presented to League of California Cities, May 4, 2011 Opening General Session ("However, until the issue is resolved, we continue to advise clients to justify and defend their ordinances as land-use controls that may be adopted based on the public health, safety, and welfare, with the nexus study providing only a backup to oppose a claim that the requirements must be justified by such a study.") (available at: http://www.cacities.org/getattachment/802e4824-6f21-4dc5-ab33-181930c230ed/5-2011-Spring-Barbara-Kautz-Life-After-Palmer_-(1).aspx); Rawson, M., *Inclusionary Housing After Palmer and Patterson: Alive & Well in California* (California Affordable Housing Law Project, May 2010) (Recommending that municipalities not revise inclusionary housing fees based on nexus studies, but continue to characterize them as police-power land-use regulations subject to deferential review under constitutions and statutes), available at: http://pilpca.org/wp-content/uploads/2010/10/Inclusionary-Zoning-After-Palmer-Patterson-7-11-10.pdf. *See also* Kautz, B., *In Defense of Inclusionary Zoning; Successfully Creating Affordable Housing,* 36 U.S.F. L. Rev. 971, 977 & 1012 (2002) (Inclusionary housing ordinances are defensible if drafted to closely resemble ordinary zoning ordinances.); California Affordable Housing Law Project and Western Center on Law and Poverty, *Inclusionary Zoning: Legal Issues,* (December 2002) (Recommending that ordinances be based on the community's need for affordable housing as evidenced by their general plan housing elements, fair-share regional housing needs, HUD data and other information.)

Patterson, that inclusionary housing requirements were not fees, dedications or other exactions subject to the statutory and constitutional constraints governing such requirements, but rather were simply land-use measures similar to other zoning regulations governing height, setbacks, etc., adopted under the local government's police power, and thus accorded a highly deferential standard of judicial review. They accordingly disclaimed any need to demonstrate any relationship—reasonable or otherwise—between the housing mitigation requirements and the deleterious impacts of residential development under *San Remo* or *Patterson.* As one widely circulated paper on the topic asserted:

> Communities and advocates must confront head-on the misplaced view advanced by some after *Patterson*—that inclusionary housing obligations and in-lieu fees are a type of exaction required to be strictly related to the projected need for new affordable housing created by new housing development rather than land use regulations related to *the community's legitimate desire to accommodate its critical existing and projected needs for affordable housing*, to provide opportunities for households of all income levels and to affirmatively further integration and other fair housing goals.[17]

Consistent with this approach, despite having commissioned and approved residential nexus studies purporting to validate inclusionary housing fees on rental housing as development exactions, these municipalities have continued to insist either that (1) their *for-sale* affordable housing set asides and in-lieu fees do not constitute development exactions, but are merely zoning regulations intended to ensure a supply of affordable housing; and/or (2) that *neither* their in-lieu fees nor their affordable housing impact fees constitute exactions subject to the reasonable-relationship standard.[18]

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[17] Rawson, *Inclusionary Housing after Palmer and Patterson* at 4 (emphasis added).

[18] The latter approach is illustrated by the City of Walnut Creek. In 2010, in the wake of the *Palmer* and *Patterson* decisions, the City commissioned a residential nexus study by Keyser Marston "to estimate and quantify the nexus between new residential development in Walnut Creek and the new demand for affordable housing that would be caused by that development." Staff Report to Walnut Creek City Council (Oct 19, 2010) at 2 (available at: http://walnutcreek.granicus.com/MetaViewer.php?view_id=2&clip_id=1182&meta_id=46724) The City's inclusionary housing ordinance, however, characterizes the fee on for-sale housing as an "in-lieu fee" and the fee on rental housing as an "impact fee." It provides that developments with for-sale units shall either set aside the number of inclusionary units or pay an in-lieu fee.

In June 2010, the Fremont City Council updated its Affordable Housing Ordinance and adopted Resolution No. 2010-35 approving in-lieu fees for for-sale housing and "affordable housing impact fees" for rental housing. The Resolution states:

> [T]he in-lieu fee option may be used only in for-sale projects and is a generally applicable menu option that may be selected by an applicant as an alternative to on-site construction. *It is not a mandated fee required as a condition to developing property, nor is it a fee subject to the analysis in Building Industry Association of Central California v. City of Patterson*, 171 Cal.App.4th 886 (2009).[19]

The Affordable Housing Ordinance amendments approved at the same time contains identical language and explains the basis for the rental impact fee as follows:

> A 2009 decision of the California Court of Appeal holds that the city may not require rents to be limited in rental projects unless the city provides assistance to the rental project. *To conform with this decision, this chapter does not require any rental project*, except those rental projects that receive city assistance, *to limit rents or to pay an in-lieu fee*. Instead, consistent with the results of the Nexus

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City of Walnut Creek Mun. Code § 10-2.3.903(A) ["ownership projects shall either include the number of inclusionary units required under Section 10-2.3.904 or, if applicable, pay the in-lieu fee required under Section 10-2.3.905]. Rental units, on the other hand, must pay an "affordable housing impact fee." *Id,* § 10-2.3.903(B) ["rental projects shall pay an affordable housing impact fee, if such a fee has been adopted, upon issuance of a building permit for each dwelling unit in the rental project."]. Yet the same ordinance states:

> Nothing in this chapter shall deem or be used to deem the impact and in-lieu fees authorized pursuant to this section as an ad hoc exaction, as a mandated fee required as a condition to developing property, or as a fee subject to the analysis in *Building Industry Association of Central California v. City of Patterson*, 171 Cal.App.4th 886 (2009). Any in-lieu fee adopted by the City Council is a menu option that may serve as an alternative to the on-site housing requirements for ownership projects set forth in this Article.

[19] Fremont City Council Resolution No. 2010-35 at 1 (emphasis added).

> Study, market-rate rental projects are required to pay an affordable housing impact fee to mitigate the impacts of those rental projects on the need for affordable housing. The affordable housing impact fee is reasonably related to the need for affordable housing associated with market-rate rental housing.[20]

Other municipalities have similar language in their inclusionary housing ordinances. *See, e.g.*, City of San José Mun. Code § 5.08.020 ("Nothing in this chapter shall deem or be used to deem the impact and in-lieu fees authorized pursuant to this section as . . . a mandated fee required as a condition to developing property, or as a fee subject to the analysis in *Building Industry Association of Central California v. City of Patterson*, 171 Cal. App. 4th 886 (2009)).")[21]

This stance, which even some municipal attorneys have acknowledged as problematic,[22] reflects the intellectual and legal tension between the effort to characterize a subset of inclusionary housing requirements as "impact fees" and the longstanding acknowledgement that affordable housing needs are generated by broader social and economic forces, not by new residential development, and should be justified based on the community's desire to provide housing for all income segments.

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[20] Fremont Municipal Code § 18.155.010 (g) (emphasis added).

[21] *See also* City of San Carlos Mun. Code § 18.16.030 (A)(4) ("Nothing in this chapter or Chapter 18.17 shall deem or be used to deem the in lieu fee authorized pursuant to subsection (A)(3) of this section as . . . as a mandated fee required as a condition to developing property, or as a fee subject to the analysis in *Building Industry Association of Central California v. City of Patterson*, 171 Cal.App.4th 886 (2009). Any in lieu fee adopted by the City Council is a menu option that may serve as an alternative to the on-site below-market-rate housing requirements set forth in this chapter."); City of Concord Dev. Code § 122-579(d)(4) (same).

[22] *See* Seltzer, A. *Home Sweet Home? Legal Challenges to Inclusionary Ordinances and Housing Elements Action Apartment Association v. City of Santa Monica,* League of California Cities Conference (Sept. 2009) (available at: http://www.cacities.org/getattachment/f40e9c19-625e-4ce3-ba6d-ccf00777d1cd/9-2009-Annual-ALAN-SELTZER_Home-Sweet-Home-Action.aspx) ("The best defense of IHOs may be for cities to characterize affordable ownership housing obligations and an "*Ehrlich*" in lieu fee for such development as traditional zoning, exempt rental housing from affordability requirements under Costa-Hawkins, and impose an MFA impact fee instead on rental housing. This strategy -- distinguishing an "*Ehrlich*" in lieu fee from an MFA impact fee – will face difficulties post- *Patterson*, as the nexus study needed to justify mitigation of rental housing impacts would likely guide and be confused with the "*Ehrlich*" inclusionary ownership housing in lieu fee.")

IV. APPLICABLE LAW

A. The Mitigation Fee Act and *San Remo*

The Mitigation Fee Act, Cal. Govt. Code, §§ 66000–66025 extensively regulates the adoption and imposition of development exactions, including requirements that the purpose of the fee must be identified with specificity, and that a "reasonable relationship" must exist between the need for and use of the exaction and the type of development project on which the exaction is imposed. Cal. Govt. Code § 66001(a)(3). Government Code § 66005 provides that when a local agency imposes any fee as a condition of approval of a development project, such a fee cannot exceed the estimated reasonable cost of providing the service or facility for which the fee is imposed. A fee or exaction that exceeds the reasonable cost of providing the facilities or services constitutes a special tax that must be expressly authorized by statute and ratified by a two-thirds vote of the electorate under article XIII A, section 4 of the California Constitution. *See* Govt. Code §§ 66014; 50076–77, 53727; *Bixel Assocs. v. City of Los Angeles*, 216 Cal. App. 3d 1208, 1220 (1989) (invaliding excessive fire hydrant fee as a special tax); *Beaumont Investors v. Beaumont-Cherry Valley Water Dist.*, 165 Cal. App. 3d 227, 238 (1984) (invalidating water system hookup fee as a special tax); *see also Shapell Indus., Inc. v. Governing Bd. of the Milpitas Unified Sch. Dist.*, 1 Cal. App. 4th 218, 235–236 (1998); *Balch Enters., Inc. v. New Haven Unified Sch. Dist.*, 219 Cal. App. 3d 783, 794–795 (1990).

As its legislative history reflects, the Mitigation Fee Act was passed by the Legislature "in response to concerns among developers that local agencies were imposing development fees for purposes unrelated to development projects." *Ehrlich*, 12 Cal. 4th 864; Sen. Local Govt.Com. Analysis of Assem. Bill No. 1600 (1987–1988 Reg.Sess.) p. 1.

The Mitigation Fee Act mandates findings concerning the link between the need for and amount of the fee and the impact of the development projects on which the fee is imposed. In particular, the local agency's governing body must adopt findings demonstrating:

1. How there is a reasonable relationship between the *need* for the public facility and the *type* of development project on which the fee is imposed.
2. How there is a reasonable relationship between the *amount* of the fee and the cost of the public facility attributable to the development upon which the fee is imposed.

Cal. Govt. Code § 66001(a)(3); *id.* at (b).[23]

[23] Government Code 66001 provides:

Thus, before imposing a fee under the Mitigation Fee Act, the local agency is charged with determining that the amount of the fee and the need for the public facility are reasonably related to the burden created by the development project. If such a fee is challenged, the local agency has the burden of producing evidence in support of its determination. *Homebuilders Assn. of Tulare/Kings Counties, Inc. v. City of Lemoore*, 185 Cal.App.4th 554, 561 (2010). The local agency must show that a valid method was used for imposing the fee in question, one that established a reasonable relationship between the fee charged and the burden posed by the development. *Shapell Industries, Inc. v. Governing Board*, 1 Cal.App.4th at 235.

In addition to its procedural requirements, the Mitigation Fee Act embodies both constitutional and statutory standards against which exactions subject to its provisions must be measured. In *Ehrlich v. City of Culver City*, 12 Cal. 4th 854, 866–67 (1996), the Court held that (1) the term "reasonable relationship" as used in the Mitigation Fee Act "embraces both constitutional and statutory meanings" and should be construed in light of both federal and state constitutional jurisprudence; and (2) that all challenges to exactions, whether on statutory or constitutional grounds, must be channeled through the administrative procedures of the Act. The Court subsequently reaffirmed, in *San Remo Hotel v. City and County of San Francisco*, 27 Cal. 4th 643, 663–664 (2002), that "[a]s a matter of both statutory and constitutional law, [exactions] must bear a reasonable relationship, in both intended use and amount, to the deleterious public impact of the development."

In *San Remo Hotel*, owners of a hotel sued to invalidate a San Francisco ordinance limiting the conversion of residential hotel rooms (usually occupied by low-income tenants) to tourist hotel

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(a) In any action establishing, . . . or imposing a fee as a condition of approval of a development project . . . the local agency shall do all of the following:
(1) Identify the purpose of the fee.
(2) Identify the use to which the fee is to be put. If the use is financing public facilities, the facilities shall be identified. That identification may, but need not, be made by reference to a capital improvement plan as specified in Section 65403 or 66002, may be made in applicable general or specific plan requirements, or may be made in other public documents that identify the public facilities for which the fee is charged.
(3) Determine how there is a reasonable relationship between the fee's use and the type of development project on which the fee is imposed.
(4) Determine how there is a reasonable relationship between the need for the public facility and the type of development project on which the fee is imposed.
(b) In any action imposing a fee as a condition of approval of a development project by a local agency on or after January 1, 1989, the local agency shall determine how there is a reasonable relationship between the amount of the fee and the cost of the public facility or portion of the public facility attributable to the development on which the fee is imposed.

rooms. The purpose of the ordinance was to preserve the availability of residential hotel rooms for the City's low-income residents who would otherwise have had no viable housing options. To achieve that goal, the ordinance required a hotel converting a residential hotel unit into a tourist unit to replace the residential unit elsewhere, pay a fee in lieu of providing the replacement unit, or take other action that would further replacement. Pursuant to the ordinance, the City issued the hotel owners a conditional use permit authorizing the conversion of hotel rooms only upon compliance with one of those alternatives.

The California Supreme Court found that, as a legislative enactment, the ordinance was subject to the reasonable relationship standard set forth in the Mitigation Fee Act, which the Court, echoing *Ehrlich*, found to embody both statutory and constitutional law principles. Under this standard, the Court held, "[a]s a matter of both statutory and constitutional law, such fees must bear a reasonable relationship, in both intended use and amount, to the deleterious public impact of the development." *Id.* at 671. The Court concluded that the housing replacement fees did bear "a reasonable relationship to loss of housing ... in the generality or great majority of cases" because (1) the conversion to tourist use directly caused the loss of residential rooms; and (2) the mitigation requirements were limited to the number of rooms lost as a result of plaintiffs' conversion. Writing separately, Justice Baxter emphasized the need to demonstrate that "(1) there is a cause-and-effect relationship between the owner's desired use of the property and the social evil that the fee seeks to remedy, and (2) the fee is reasonably related in both intended use and amount to that social evil." 27 Cal. 4th at 687 (Baxter, J. concurring and dissenting)

The court in *Building Industry Association v. Patterson*, 171 Cal. App. 4th 886, applied these standards in evaluating the inclusionary housing fee under review:

> The affordable housing in-lieu fee challenged here is not substantively different from the replacement in-lieu fee considered in *San Remo*. Both are formulaic, legislatively mandated fees imposed as conditions to developing property, not discretionary ad hoc exactions. (*San Remo*, 27 Cal.4th at 671) We conclude, for this reason, that the level of constitutional scrutiny applied by the court in San Remo must be applied to City's affordable housing in-lieu fee . . . ."

Under this standard, the court ruled, the in-lieu fee could not be sustained unless there was "a reasonable relationship between the amount of the fee, as increased, and "the deleterious public impact of the development." *Id.* (citing *San Remo*, 27 Cal. 4th at 671). The court conducted a careful evaluation of the Fee Justification Study relied on by the City and concluded that it showed no reasonable relationship between the extent of City's affordable housing need and residential development. Accordingly, the court held, the Fee Justification Study did not "support

a finding that the fees bore any reasonable relationship to any deleterious impact associated with the project."

B. Inclusionary Zoning Requirements.

The California Supreme Court's recent decision in *Sterling Park, L.P. v. City of Palo Alto,* 57 Cal.4th 1193 (2013), strongly suggests that inclusionary housing requirements -- which mandate set-aside of a certain portion of new homes for sale a below-market prices -- must likewise be justified under the Mitigation Fee Act.

Sterling Park involved a condition requiring a developer to set aside ten condominium units as below-market rate housing and make a substantial cash payment to a city fund. The developer proceeded with the construction but challenged these requirements under the provisions of the Mitigation Fee Act that permit a developer to proceed with a project while "protest[ing] the imposition of any fees, dedications, reservations, or other exactions imposed on a development project." (Gov't Code § 66020, subd. (a)). The Court was required to determine "whether the requirements at issue constitute the imposition of 'any fees ... or other exactions' under [the Mitigation Fee Act]" or whether the requirements were merely police-power zoning regulations, as urged by the City.

Relying heavily on *Trinity Park, LP v. City of Sunnyvale,* 193 Cal.App.4th 1014 (2011), the court of appeal in *Sterling Park* concluded that the inclusionary requirements did not constitute exactions under the Mitigation Fee Act. *Trinity Park* had held that an affordable housing requirement of the City of Sunnyvale was not an exaction under the Mitigation Fee Act because it was not levied to help defray the costs of public infrastructure or facilities. The court of appeal rejected the plaintiff's argument that the case was distinguishable from *Trinity Park* because the challenged ordinance expressly stated that one of its purposes was to offset the demand for housing created by new development. The court dismissed this stated objective as irrelevant, reasoning that "[t]he only way a housing development could create a demand for housing would be if the new development eliminated existing housing." *Sterling Park v. City of Palo Alto*, 2012 WL 2899370 (Cal. App. 6th Dist. 2013), *review granted and depublished, Sterling Park, L.P. v. City of Palo Alto*, 57 Cal.4th 1193 (2013). The court concluded that it need not decide whether an exaction imposed to offset lost housing -- such as the one at issue in *San Remo* -- could be subject to the Act because plaintiffs' project had not demolished existing housing.

The California Supreme Court granted review and reversed. The Court concluded that *Sterling Park* had accorded an unduly narrow interpretation to the Mitigation Fee Act under which "a developer may pay under protest a fee charged to defray the cost of facilities related to the development and then challenge the fee as excessive while proceeding with the development; but it may *not* so challenge any *other* fee or exaction." *Id.* at 1205 (emphasis in original). The Court

stated that the term "other exactions" should be interpreted broadly, noting that it "at least includes actions that divest the developer of money or a possessory interest in property . . . ." The Court observed that "the Legislature was not concerned merely about excessive fees but also about 'fees for purposes unrelated to' the project. (*Ehrlich v. City of Culver City, supra*, 12 Cal.4th at p. 864 . . . .)" *Id. Trinity Park*'s interpretation, the Court continued,

> would mean section 66020 does not apply to fees imposed for purposes entirely unrelated to the project. Under that interpretation, if a fee or other exaction is not merely excessive but truly arbitrary, the developer would either have to pay it with no recourse, or delay the entire development to challenge the fee or exaction. In other words, the more unreasonable the fee or exaction, the less recourse the developer would have. This perverse interpretation is not only contrary to legislative intent, it is contrary to the broad language—"any fees, dedications, reservations, or other exactions"—the Legislature used in defining section 66020's reach.

The Court also rejected the City's contention that the requirements of its inclusionary program were not exactions but merely land-use regulations, not subject to the Mitigation Fee Act. The inclusionary program, the Court stated, was different from a land-use regulation -- such as a limit on the number of units that can be built. The two options offered under the program -- setting aside units for sale at below-market rates or paying an in-lieu fee -- both constituted "exactions" under the broad language of the Mitigation Fee Act. *Id.* at 1207. "[T]he requirement that the developer sell units below-market rate, include[ing] the City's reservation of an option to purchase the below-market rate units, is similar to a fee, dedication, or reservation." *Id.* A purchase option, the Court pointed out, was "a sufficiently strong interest in the property to require compensation if the government takes it in eminent domain." *Id.*, citing *County of San Diego v. Miller*, 13 Cal.3d 684, 691–693 (1975). Compelling the developer to give the City a purchase option thus constituted "an exaction under section 66020." *Id.*

The Court reserved, however, the specific question whether requiring developers to sell units at below-market rates *without* reserving a purchase option would constitute an exaction subject to the Mitigation Fee Act:

> It may be, as the City argues, that under traditional property law, an option to purchase creates no estate in the land. But a purchase option is a sufficiently strong interest in the property to require compensation if the government takes it in eminent domain. (*County of San Diego v. Miller* (1975) 13 Cal.3d 684, 691–693.) Compelling the developer to give the City a purchase option is an

> exaction under section 66020. Because of this conclusion, we need not decide whether forcing the developer to sell some units below market value, by itself, would constitute an exaction under section 66020.

57 Cal.4th at 1207 (emphasis added).

This issue is among those currently before the court in *California Building Industry Assn. v. City of San Jose* (Cal. App. 6th Dist. 2013) 2013 Cal. App. LEXIS 447, 2013 WL 2449204, *formerly published at* 216 Cal. App. 4th 1373. Assuming, as is probable, that the court adheres to its broader holding in *Sterling Park* that affordable housing requirements constitute exactions, inclusionary set-aside requirements will also be subject to the Mitigation Fee Act.

C. The Constitutional Overlay – The Fairness Principle

In *Palazzolo v. Rhode Island*, the Supreme Court explained that analysis of issues arising under the Takings Clause must be "informed by the *purpose* of the Takings Clause, which is to prevent the government from 'forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.'" 533 U.S. 606, 618–619 (2001) (quoting *United States v. Armstrong*, 364 U.S. 40, 49 (1960)) (emphasis added); *accord*, *Lockaway Storage v. County of Alameda*, 216 Cal. App. 4th 161, 183 (2013) ("The takings clause precludes the Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole."); *Dep't of Fish and Game v. Superior Court*, 197 Cal. App. 4th 1323, 1359 (2011) (Not forcing a few to bear burdens that in fairness and justice should be borne by the public is the "ultimate goal" of the takings clause).

The Court has applied this fairness principle to development exactions as a special application of the "unconstitutional conditions" doctrine. *Lingle v. Chevron USA. Inc.*, 544 U.S. 528, 547 (2005); *Dolan v. City of Tigard*, 512 U.S. at 385; *Nollan*, 483 U.S. at 837. Under this "well-settled doctrine" (*Dolan*, 512 U.S. at 385), a state may not condition the grant of a license, permit or other benefit on the recipient's surrender of a constitutional right.[24] The Supreme Court

[24] The doctrine has been applied in a variety of contexts, including First Amendment freedom of speech (*Agency for International Development v. Alliance for Open Society International, Inc.*, 133 S. Ct. 2321 (2013) [requirement that recipient organizations adopt policy explicitly opposing prostitution to receive federal funding to provide HIV and AIDS programs was unconstitutional condition under First Amendment]); freedom of religion (*Sherbert v. Verner*, 374. U.S. 398 (1963) [state could not deny unemployment benefits to woman whose religion forbade working on the Sabbath]); right of interstate travel (*Shapiro v. Thompson*, 394 U.S. 618 (1969) [conditioning of welfare benefits upon minimum of one year in-state residency penalized

recently described this as an "overarching principle" under which "government may not deny a benefit to a person because he exercises -- or, as in this case, refuses to surrender -- a constitutional right." *Koontz v. St. Johns River Water Management District*, 133 S.Ct. 2586, 2594 (2013). The doctrine "vindicates the Constitution's enumerated rights by prohibiting the government from coercing people into giving them up." *Id; see also, Perry v. Sinderman,* 408 U.S. 593, 597 (1972) ("[E]ven though a person has no 'right' to a valuable governmental benefit and even though the government may deny him the benefit for any number of reasons, there are some reasons upon which the government may not rely. It may not deny a benefit to a person on a basis that infringes his constitutionally protected interests . . . .")

Both the fairness principle and the unconstitutional conditions doctrine come into play when a condition or exaction imposed in the development approval context lacks a reasonable relationship with the impact of the development. Courts routinely uphold laws requiring property owners to pay fees or bear other exactions when their actions can reasonably be established as the proximate cause of the social problem to be remedied and the fees or exactions are reasonable in relation to the extent of the development's contribution to problem. But where use of property cannot reasonably be shown to be the proximate cause of the problem sought to be addressed, or the exaction is disproportionate to the impact of that use, the regulation runs afoul of both the fairness principle and the unconstitutional conditions doctrine and will be set aside. *See, e.g., Koontz v. St. Johns River Water Mgmt. Dist*, 133 S.Ct. 2586, 2601 (2013) (Government may require permit applicant to mitigate the impacts of a proposed development but may not use leverage to go beyond constitutionally established limitations); *Del Monte Dunes v. City of Monterey*, 95 F.3d 1422, 1432 (9th Cir. 1996) (invalidating dedication requirement that was disproportionate to the impact that the property development caused); *Surfside Colony, Ltd. v. Cal. Coastal Comm'n*, 214 Cal. App. 3d 1260, 1269 (1991) (required dedication of a public access to a private beach was unconstitutional because there was no causal nexus between the dedication and the problem of beach erosion); *Rohn v. City of Visalia*, 214 Cal. App. 3d, 1457–57 (1989) (conditioning issuance of building permit on dedication of land for a road improvement was a taking because the development did not cause traffic problems).

Application of the fairness principle in the context of development exactions was explained in *Shapell Indus., Inc. v. Governing Bd. of the Milpitas Unified Sch. Dist.*, 1 Cal. App. 4th 218, 235–236 (1998):

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fundamental right of interstate travel]); and Fifth Amendment property rights (*Nollan v. California Coastal Commission*, 483 U.S. 825 (1987) [Coastal Commission could not condition building permit on grant of a lateral beach access easement unrelated to the impact of the new construction]).

> While it is "only fair" that the public at large should not be obliged to pay for the increased burden on public facilities *caused by new development*, the converse is equally reasonable: the developer must not be required to shoulder the entire burden of financing public facilities for all future users. "[T]o impose the burden on one property owner to an extent beyond his [or her] own use shifts the government's burden unfairly to a private party...." (*Liberty v. California Coastal Com.* (1980) 113 Cal.App.3d 491, 504, 170 Cal.Rptr. 247, fn. omitted.) It follows that facilities fees are justified only to the extent that they are limited to the cost of increased services *made necessary by virtue of the development.* (*Trent, supra*, 114 Cal.App.3d 317, 170 Cal.Rptr. 685; *Russ Bldg. Partnership v. City and County of San Francisco* (1987) 199 Cal.App.3d 1496, 1506, 246 Cal.Rptr. 21. The Board imposing the fee must therefore show that a valid method was used for arriving at the fee in question, "one which established a reasonable relationship between the fee charged and the burden posed by the development." (*Bixel Associates v. City of Los Angeles* (1989) 216 Cal.App.3d 1208, 1219, 265 Cal.Rptr. 347; *Jones, supra*, 157 Cal.App.3d 745, 203 Cal.Rptr. 580.) (emphases added)

As the California Supreme Court confirmed in *Ehrlich*, this principle extends beyond financing of public facilities to include any exactions imposed as a condition of approval of development "that divest the developer of money or a possessory interest in property." 12 Cal. 4th at 864. As is also clear from *Koontz v. St. Johns River Water Management District*, 133 S.Ct. 2586 (2013), the principle applies to monetary exactions as well as conditions directly involving real property interests.

D. Applicability of *Nollan/Dolan* Doctrines.

A major issue left open by *Koontz,* was whether its determination that the unconstitutional conditions doctrine underpinning *Nollan* and *Dolan* applied to monetary exactions required use of the *Nollan/Dolan* nexus and rough proportionality standards in evaluating legislatively enacted monetary exactions as well as *ad hoc* requirements.[25]

[25] The Supreme Court has not drawn any distinction between legislative and ad hoc requirements in applying the unconstitutional conditions doctrine. *See, e.g., United States v. American Library Association, Inc.*, 539 U.S. 194 (2003).

Decisions in the Ninth Circuit since *Koontz* confirm that it does. In *Horne v. U.S. Dept. of Agriculture*, 750 F.3d 1128 (9th Cir. 2014), the court concluded that the nexus and rough proportionality standards applied to a takings challenge to a USDA order that applied uniformly to all raisin producers under Agricultural Marketing Agreement Act of 1937. The marketing order -- originally issued in 1939 -- required raisin producers to convey a certain portion of their annual crop to the Raisin Administrative Committee (RAC) to stabilize market prices. Plaintiffs argued that this requirement worked a constitutional taking by depriving raisin producers of their personal property, the diverted raisins, without just compensation. They effectively refused to divert the specified percentage of their crop, which resulted a penalty imposed by the Secretary of Agriculture in the amount of the market value of the unreserved raisins

The Ninth Circuit began its analysis by noting that "*Koontz* confronts the issue of how to analyze a takings claim when a 'monetary exaction,' rather than a specific piece of property, is the subject of that claim." *Id.* at 1137. "This direct linkage," the court stated "between the monetary exaction and the piece of land guided the Court [in *Koontz*] to invoke the substantive takings jurisprudence relevant to the *land* for the purpose of determining whether the related *monetary exaction* constituted a taking." *Id.* (emphasis original). The instant case, the court continued, implicated the unconstitutional conditions doctrine in the same manner as in *Koontz*:

> The Hornes faced a choice: relinquish the raisins to the RAC or face the imposition of a penalty . . . . . Because the Marketing Order is structured in this way, we follow *Koontz* to analyze the constitutionality of the penalty imposed on the Hornes against the backdrop of the reserve requirement. If the Secretary works a constitutional taking by accepting (through the RAC) reserved raisins, then, under the unconstitutional conditions doctrine, the Secretary cannot lawfully impose a penalty for non-compliance.

Id. at 1138.

After reviewing *Nollan* and *Dolan* cases, the court concluded that the nexus and rough proportionality analysis applied "because we believe it serves to govern this use restriction as well as it does the land use permitting process." *Id.* The court found "important parallels between *Nollan* and *Dolan* on one hand and the raisin diversion program on the other:"

> All involve a conditional exaction, whether it be the granting of an easement, as in *Nollan;* a transfer of title, as in *Dolan;* or the loss of possessory and dispositional control, as here. All conditionally grant a government benefit in exchange for an exaction. And, critically, all three cases involve choice. Just as the Nollans could have continued to lease their property with the existing bungalow

> and Ms. Dolan could have left her store and unpaved parking lot as they were, the Hornes, too, can avoid the reserve requirement of the Marketing Order by, as the Secretary notes, planting different crops, including other types of raisins, not subject to this Marketing Order or selling their grapes without drying them into raisins. Given these similarities, we are satisfied the rule of *Nollan* and *Dolan* governs this case.

Id. at 1142.

That *Dolan* involved an adjudicative rather than legislative decision, the court found, did not preclude application of the rough proportionality analysis. *Id.* Employing that analysis, the court ultimately concluded that the government's annual review and tying of the reserve requirement to market and industry conditions was enough to ensure that the requirement was roughly proportional to its goals. *Id.* at 1144.

The *Nollan/Dolan* analysis was employed by the court in *Levin v. City & County of San Francisco*, No. 3:14-CV-03352-CRB, 2014 WL 5355088 (N.D. Cal. Oct. 21, 2014), in striking legislatively imposed tenant relocation payments required under San Francisco's rent control ordinance. At issue in *Levin* were relocation payments required by 2014 amendments to the ordinance. Under the amended ordinance, in order to withdraw a rental unit under the Ellis Act, property owners were required to pay the greater of the lump sum required under the original ordinance or an amount equal to twenty-four times the difference between the unit's current monthly rate and the fair market value of a comparable unit in San Francisco. Plaintiffs brought a facial challenge to the 2014 ordinance as a violation of the Takings Clause.

The court held that under *Nollan*, *Dolan* and *Koontz*, the San Francisco ordinance effected "an unconstitutional taking by conditioning property owners' right to withdraw their property on a monetary exaction not sufficiently related to the impact of the withdrawal." *Id.* at 1. The court found that *Koontz* provided the "critical conceptual link between *Nollan/Dolan* and the challenged Ordinance" because the tenant relocation payments burdened ownership of a specific parcel of land. *Id.* at 7 Based on that link, the court reasoned, the relocation payment requirement "implicate[d] the central concern of *Nollan* and *Dolan*: the risk that the government may use its substantial power and discretion in land-use permitting to pursue governmental ends that lack an essential nexus and rough proportionality to the effects of the proposed new use of the specific property at issue, thereby diminishing without justification the value of the property." *Id.*

The court also found in the case the same parallels that encouraged the Ninth Circuit to apply the *Nollan/Dolan* rule to the challenged Marketing Order in *Horne,* 750 F.3d at 1142–43:

> As in *Nollan*, *Dolan*, and *Horne*, the challenged Ordinance requires a conditional exaction: the loss of substantial funds or physical control over the landlord's unit. *See Horne*, 750 F.3d at 1143. All conditionally grant a government benefit in exchange for the exaction, which here takes the form of the Ellis Act permit that the landlord must have in order to withdraw property from the rental market. *See id.* at 1143. And, critically, all of these cases involve choice: the Nollans could have continued to lease their property with the existing structure, Ms. Dolan could have left her store and parking lot unchanged, the Hornes could have avoided the Marketing Order by planting different crops, and the Levins and Park Lane can avoid paying the exaction by subjecting their property to continued occupation by an unwanted tenant.

Id. at 8. The court found that the challenged ordinance implicated the core concern of *Nollan* and *Dolan* "as acutely and in the same way as the traditional land-use permitting context: the risk that San Francisco has used its substantial power under the Ellis Act to pursue policy goals that lack an essential nexus and rough proportionality to the effects of a property owner withdrawing a unit from the rental market." *Id.* at 7.

The court rejected the City's contention that *Nollan/Dolan* did not apply to legislatively imposed conditions in reliance on *McClung v.* City *of Sumner,* 548 F.3d 1219 (9th Cir.2008). "*Koontz,*" the court stated "abrogated *McClung's* holding that *Nollan/Dolan* does not apply to monetary exactions, which is intertwined with and underlies *McClung's* assumptions about legislative conditions." *Id.* at 6, n.4. The court also observed that the Ninth Circuit's decision in *Horne,* "reinforces the applicability of the *Nollan/Dolan* framework to facial reviews of legislative exactions." *Id.*

Turning to the evaluation under the *Nollan/Dolan* framework, the court held that the ordinance on its face failed both the essential nexus and rough proportionality tests. *Id.* at 9. The ordinance required property owners seeking a permit to pay the tenant the equivalent of two years' worth of the alleged gap between the reduced rent the tenant was paying the property owner and the market rent for a comparable unit. The City argued that the necessary nexus thus existed because the eviction was the cause of the tenant being exposed to unaffordably high market rents, hence the requirement that the property owner pay for two years of that rent differential. The court emphatically rejected this argument, pointing out that the property owner's decision to repossess a unit did not *cause* the rent differential gap to which the tenant was exposed. Rather, this was the result of two variables -- market rental rates and rent controlled rates -- neither of which was attributable to the property owner. The market rate, the court observed, was the result of limited supply and the correspondingly high price. of rental units in San Francisco caused by entrenched

market forces and structural decisions made by the City long ago in the management of its housing stock. *Id.* at 9. And the rental rate was the result of the City's regulatory requirements.

It followed, the court reasoned, that *Dolan's* rough proportionality requirement could not be satisfied:

> The market effect of an Ellis Act withdrawal—indeed, of all Ellis Act withdrawals, which number on the order of a few dozen every year among a housing stock of hundreds of thousands of units—is infinitesimally small. . . . Against the infinitesimally small impact of the withdrawal on the rent differential gap to which a tenant might now be exposed, the Ordinance requires an enormous payout untethered in both nature and amount to the social harm actually caused by the property owner's action.

Id. at 9-10.

The court acknowledged that San Francisco's housing shortage and high market rates were matters of serious public concern, and found the City's efforts to address them laudable. But the City could not constitutionally accomplish its objectives by placing the onus of this problem on landlords in the absence of the required nexus and rough proportionality:

> The Constitution prohibits the City from taking the policy shortcut it has taken here, in which the City seeks to 'forc[e] some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.' [Citations omitted] . . . . In so doing, the City has crossed the constitutional line between permissible government regulation of land and an impermissible monetary exaction that lacks an essential nexus and rough proportionality to the impact of an Ellis Act withdrawal.

Id. at 13.

E. The Causal Connection – Proximate and Substantial

Central to the requirements of *San Remo* and the Mitigation Fee Act is a showing of the reasonable *causal* relationship between the proposed development and the problem the exaction is designed to address. *San Remo Hotel,* 27 Cal. 4th at 664 (an exaction "must bear a reasonable relationship, in both intended use and amount, to the deleterious public impact of the development"). The mandate that the fee be "reasonably *related,*" according to its plain meaning, requires a reasonable causal connection or link between the development and the impact sought

to be addressed.[26] *See Homebuilders Ass'n of Tulare/Kings Counties, Inc. v. City of Lemoore*, 185 Cal.App.4th 554, 576 (2010) (Ardaiz, J. concurring) ("Section 66000 and 66001 refer to a fee related to the development project. The term 'related' would in its normal usage mean associated with or having a close connection to. I would infer from this that the proposed specific project or class of projects must be a consequence of or have a direct relationship to the proposed development.") (Citation omitted).

In the inclusionary housing context, the causation element is essential to the required finding of a reasonable relationship between the type of development and the existence and extent of the need for affordable housing. If no reasonable causal connection exists between new residential development and affordable housing needs, the agency cannot sustain the burden of establishing that there is a reasonable relationship between (1) the development and the *need* for affordable housing; (2) the development and the *use* of the exaction to provide affordable housing; or (3) the amount or extent of the exaction and the *cost* of the affordable housing attributable to the development. Cal. Govt. Code §§ 66001(a)(3)–(4); *id.* at (b). Nor can the agency meeting the essential nexus and rough proportionality standards of *Nollan* and *Dolan* that are incorporated into the Mitigation Fee Act's requirements. *See Ehrlich v. City of Culver City*, 12 Cal. 4th 854, 866–67 (1996) (Term "reasonable relationship" as used in Mitigation Fee Act "embraces both constitutional and statutory meanings" and should be construed in light of both federal and state constitutional jurisprudence). Without that fundamental causal connection, the exaction becomes an unconstitutional condition.

(1) Proximate Cause in the Takings Context.

Proximate cause analysis, which is routinely employed by courts in a wide variety of contexts including takings law, is appropriate to the determination whether the causal component of the reasonable-relationship standard is satisfied. Proximate causation reflects both "'ideas of what justice demands'" and "'of what is administratively possible and convenient,'" *Anza v. Ideal Steel Supply Corp.*, 57 U.S. at 458 (quoting *Prosser & Keeton* § 41, at 264). The proximate cause inquiry works toward answering the constitutional question reflected in the reasonable-relationship test—whether the development is sufficiently connected with the social problem to make it fair and reasonable to require the property owner—as opposed to society as a whole—to address it through mitigation.

In the regulatory takings context, the Supreme Court has stated that courts will use proximate cause concepts to determine if the government regulation caused the property owners' losses:

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[26] *See* Merriam Webster Dictionary ["**related**: 1. connected by reason of an established or discoverable relation" http://www.merriam-webster.com/dictionary/related.

> [W]e have frequently observed that whether a particular restriction will be rendered invalid by the government's failure to pay for any losses *proximately caused by it* depends largely upon the particular circumstances in that case. (Emphasis added)

Penn. Cent. Transp. Co. v. New York City, 438 U.S. 104, 124 (1978) (quoting *United States v. Cent. Eureka Mining Co.*, 357 U.S. 155, 168 (1958); *see also Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 344–45 (2002) ("[O]rdinary principles of proximate cause govern the causation inquiry for takings claims.") (Rehnquist, J. dissenting). In *Esplanade Props., LLC v. City of Seattle*, 307 F.3d 978, 984 (9th Cir. 2002), the court, confirming that plaintiffs in a takings claim must establish proximate causation, recognized that "little discussion of a 'causation' requirement in any of the case law involving regulatory takings" is "due to nothing more than the fact that, in most regulatory takings cases, there is no doubt whatsoever about whether the government's action was the cause of the alleged taking."

The use of the proximate cause in cases arising under the Takings Clause has also been explicitly endorsed by the California Supreme Court. *See, e.g.*, *Locklin v. City of Lafayette*, 7 Cal.4th 327, 368 (1994); *Belair v. Riverside County Flood Control Dist.*, 47 Cal. 3d 559 (1988); *Albers v. County of Los Angeles*, 62 Cal. 2d 250, 262 (1965) ("[A]ny actual physical injury to real property proximately caused by the improvement . . . is compensable under article 1, section 14 . . . ."). This principle has been widely cited by California courts in inverse condemnation cases involving public improvements.

California courts have also emphasized the close connection between the proximate cause requirement and the constitutional fairness doctrine, which holds that property owners should not have to bear burdens that, in fairness, should be borne by society. Courts have referred to this policy as the "loss distribution' premise." *See Holtz v. Superior Court* (1970) 3 Cal. 3d 296, 303–304. *See also Pac. Bell v. City of San Diego*, 81 Cal. App. 4th 596, 607 (2000) ("[T]he fundamental policy underlying inverse condemnation is to distribute the costs of the public benefit among those benefited by the public improvement rather than imposing a disproportionate burden on the person damaged by the operation of the improvement.") The California Supreme Court has explained that, in takings cases, the "general rule of compensability [does] not derive from statutory or common law tort doctrine, but instead [rests] on the construction ... of our constitutional provision . . . Article I, section 14:"

> The decisive consideration is whether the owner of the damaged property if uncompensated would contribute more than his proper share to the public undertaking. In other words, the underlying purpose of our constitutional provision in inverse—as well as ordinary—condemnation is to distribute throughout the community the loss inflicted upon the individual by the making of public

> improvements: to socialize the burden . . . —to afford relief to the landowner in cases in which it is unfair to ask him to bear a burden that should be assumed by society.

3 Cal. 3d 296 at 303 (citations omitted); *see also Albers v. County of Los Angeles,* 62 Cal.2d 250, (1965) (Fundamental policy basis for the constitutional requirement of just compensation is a consideration of "whether the owner of the damaged property if uncompensated would contribute more than his proper share to the public undertaking.")

In *Belair v. Riverside County Flood Control Dist.*, 47 Cal. 3d 550, 558–59 (1988), the Court confirmed that inverse condemnation liability requires a showing of proximate cause, and clarified that this required a showing of "a *substantial* cause-and-effect relationship excluding the probability that other forces alone produced the injury." (Emphasis added) Under this test, when the activity in question merely contributes to the injury, proximate cause is established only if the injury occurred in substantial part because of the activity. *Id.* at 559–560; *accord*, *Biron v. City of Redding*, 225 Cal. App. 4th 1264, 1279 (2014); *Souza v. Silver Dev. Co.*, 164 Cal. App. 3d at 171; *Gutierrez v. County of San Bernardino*, 198 Cal. App. 4th 831, 836 (2011) ("To be a proximate cause, the design, construction or maintenance of the improvement must be a substantial cause of the damage.").

(2) Proximate Cause in Other Contexts.

Courts have also employed proximate cause principles in other non-tort contexts, using the same standards of reasonableness and fairness to place limits on the extent to which a party will be held legally liable or responsible for an alleged impact. For example, the Supreme Court has held that proximate cause principles are appropriate to limit the scope of liability for antitrust violations. *Associated General Contractors of California, Inc. v. California State Council of Carpenters*, 459 U.S. 519, 535–536 (1983). In holding that the plaintiffs could not maintain their antitrust action, the high court stressed, among other factors, the "indirectness of the asserted injury." 459 U.S. at 540. Focusing on the "chain of causation" between the plaintiffs' injury and the alleged antitrust violation, the Court found "that any such injuries were only an indirect result of whatever harm may have been suffered" by parties that lost business due to the defendants' conduct. *Id.* at. 540–541.

The Supreme Court has also used the proximate cause concept to limit the reach of impacts that agencies must consider (and that project proponents must provide mitigation for) under the National Environmental Protection Act ("NEPA"). *See, e.g., Dep't of Transp. v. Pub. Citizen*, 541 U.S. 752, 767 (2004) (analogizing "reasonably close causal relationship" inquiry for defining "indirect effects" in NEPA context to proximate cause inquiry in tort law, and holding

that an agency with no discretion or ability to prevent a certain effect due to its limited statutory authority, cannot be considered a legally relevant "cause" of the effect).[27]

In *Metropolitan Edison Co. v. People Against Nuclear Energy*, 460 U.S. 766, 774 (1983), the Court invoked proximate cause concepts in holding, under NEPA, that the Nuclear Regulatory Commission did not have to consider whether the risk of nuclear accident would cause harm to psychological health and well-being of community surrounding nuclear plant because "the element of risk lengthens the causal chain beyond the reach of NEPA." The Court reasoned that NEPA requires "a reasonably close causal relationship between a change in the physical environment and the [prospective] effect at issue," which it interpreted as being "like the familiar doctrine of proximate cause from tort law." 460 U.S. at 776 (citing W. Prosser, *Law of Torts* ch. 7 (4th ed. 1971)). This was necessary to limit the drain on "time and resources" that would result if an agency were forced to examine attenuated effects. *Id.* at 774. The Court subsequently reiterated, in *Department of Transportation v. Public Citizen*, 541 U.S. 752 (2004), that "a 'but for' causal relationship is insufficient to make an agency responsible for a particular effect," 541 U.S. at 767, and therefore insufficient to require the agency to analyze that effect under NEPA.

The application of proximate cause in NEPA is particularly instructive for development fees and exactions. Both NEPA and exactions place obligations on parties to mitigate for the possible effects of their actions. In both of these contexts, the prudential limitations of proximate cause are necessary to "draw a manageable line between those causal changes that may make an actor responsible for an effect and those that do not." *Dep't of Transp. v. Pub. Citizen*, 541 U.S. at 767.

Courts have also imported the proximate cause concept into the Endangered Species Act ("ESA") to place a reasonable limit on the imposition of legal responsibility on property owners for the impacts of their land-use activities on threatened and endangered species. *Babbitt v. Sweet Home Communities.*, 515 U.S. 687 (1995).[28] *Sweet Home* involved § 9 of the ESA, which forbids

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[27] Federal courts have also employed proximate cause principles in applying other environmental statutes. *See, e.g.*, *United States* v. *West of Eng. Ship Owner's Mut. Prot. & Indem. Ass'n (Lux.)*, 872 F.2d 1192, 1198–1200 (5th Cir. 1989) (Federal Water Pollution Control Act); *Benefield v. Exxon Corp.*, 959 F.2d 805, 807 (9th Cir. 1992) (Trans-Alaska Pipeline Authorization Act).

[28] In *Cascadia Wildlands v. Kitzhaber*, 911 F. Supp. 2d 1075, 1084 (D. Or. 2012), in concluding that a plaintiffs' ESA claim lacked the necessary showing of proximate cause, the court stated:

the "take" of an endangered or threatened species. Although this provision does not expressly use the terms "cause" or "proximate cause," the Court found it appropriate to use "ordinary requirements of proximate causation and foreseeability." 515 U.S. at 697 n.9. Both the concurring and dissenting opinions agreed that the use of proximate cause principles was appropriate in the ESA context to cut off property owner responsibility in the face of a lengthy chain-of-events theory of liability. 515 U.S. at 712 (O'Connor, J., concurring); *id.* at 732 (Scalia, J., dissenting) ("I quite agree that the statute contains" a proximate cause requirement.). As Justice O'Connor further explained, application of proximate cause "depends to a great extent on considerations of the fairness of imposing liability for remote consequences." *Id.*

A recent and instructive example of the use of proximate cause in the ESA context occurred in *The Aransas Project v. Shaw*, No. 13-40317, 2014 WL 2932514 (5th Cir., June 30, 2014). There, the Fifth Circuit Court of Appeals held that the Texas Commission on Environmental Quality ("TCEQ") was not responsible for the deaths of endangered whooping cranes based on issuance of permits to withdraw water from rivers that sustained whooping crane habitat, finding that "the district court either misunderstood the relevant liability test or misapplied proximate cause when it held the state defendants responsible for remote, attenuated, and fortuitous events following their issuance of water permits."

The appellate court emphasized that "[p]roximate cause and foreseeability are required to affix liability for ESA violations," and observed that "[n]owhere does the [district] court explain why the remote connection between water licensing, decisions to draw river water by hundreds of users, whooping crane habitat, and crane deaths that occurred during a year of extraordinary drought compels ESA liability." It reliance on *Sweet Home*, the court rejected the lower court's causation analysis, concluding that "[t]he lack of foreseeability or direct connection between TCEQ permitting and crane deaths is also highlighted by the number of contingencies affecting the chain of causation from licensing to crane deaths. The contingencies are all outside the state's control and often outside human control." These included water use by and availability from other sources, and "even more unpredictable and uncontrollable" forces of nature, including "weather, tides and temperature conditions," which "dramatically affect[ed]" conditions in the subject estuary. The court concluded that "[f]inding proximate cause and imposing liability on the state defendants in the face of multiple, natural, independent, unpredictable and interrelated forces affecting the cranes' estuary environment goes too far."

> To establish proximate causation, plaintiffs must still present a direct relation between the injury asserted and the injurious conduct alleged, and the link between the two cannot be too remote, purely contingent, or indirect.

Like NEPA and the ESA, CEQA limits the range of impacts that agencies must consider and mitigate and these limits have incorporated proximate cause principles. CEQA does not require agencies to consider impacts that speculative or unlikely to occur. 14 Cal. Code Regs. § 15143; 15145. *See Residents Ad Hoc Stadium Comm. v. Bd. of Trustees*, 89 Cal. App. 3d 274, 287 (1979); *see also Friends of the Eel River v. Sonoma County. Water Agency*, 108 Cal. App. 4th 859, 875 (2003) (The possibility that project approval might affect future action by another agency on a different proposal need not be analyzed under CEQA).

(3) Proximate Cause Standards

Proximate cause analysis has two components, both of which must be established for a legally sustainable relationship to exist. *Jackson v. Ryder Truck Rental, Inc.*, 16 Cal. App. 4th 1830 (1993). The first question is whether there is a *substantial* cause-and-effect relationship between the act or omission and the harm. *Mitchell v. Gonzales*, 54 Cal. 3d 1041, 1049 (1991), "The proper rule for such situations is that the defendant's conduct is a cause of the event because it is a material element and a substantial factor in bringing it about." *Id.* at 1052; *Vecchione v. Carlin*, 111 Cal. App. 3d 351, 359 (1980); Prosser & Keeton on Torts (5th ed. 1984) § 41, pp. 266–267. The second issue is whether the party's conduct was closely enough related to the harm that the defendant *should* be held responsible. "This second component of proximate cause, which asks a policy question, has been termed the 'normative or evaluative element' of proximate cause. *Jackson v. Ryder Truck Rental, Inc.*, 16 Cal. App. 4th at 1847 (quoting *Mitchell v. Gonzalez,* 54 Cal. 3d at 1056 (1991) (Kennard, J. dissenting); *see also Evan F. v. Hughson United Methodist Church*, 8 Cal. App. 4th 828, 834–835 (1992).

In *PPG Industries v. Transamerica Insurance Co.*, 20 Cal. 4th 310 (1999), the California Supreme Court explained that the reason for the second component is that without some policy limitation on legal responsibility, the chain of causation can stretch both backwards and forwards, potentially resulting in unlimited liability. *Id.* at 315. The Court quoted with approval Justice Traynor's observation that proximate cause "is ordinarily concerned, not with the fact of causation, but with the various considerations of policy that limit an actor's responsibility for the consequences of his conduct." *Id.* quoting *Mosley v. Arden Farms Co.*, 26 Cal. 2d 213, 221 (1945) (Traynor, J., concurring).

Proximate cause has been employed so widely for so long because, as both the Supreme Court and the California Supreme Court have recognized, the alternative—mere "but-for" causation—is no alternative at all because "'the consequences of an act go forward to eternity, and the causes of an event go back to the dawn of human events, and beyond.'" *Exxon Co., U.S.A. v. Sofec, Inc.*, 517 U.S. 830, 838 (1996) (quoting W. Keeton et al., *Prosser and Keeton on the Law of Torts* § 41, at 266 (5th ed. 1984)); *PPG Indus.*, 20 Cal. 4th at 324.

"The chief and sufficient reason for [proximate cause] is to be found in the impossibility of tracing consequences through successive steps to the remote cause, and the necessity of pausing in the investigation of the chain of events at the point beyond which experience and observation convince us we cannot press our inquiries with safety." *Associated Gen. Contractors of Cal.*, 459 U.S. 519, 532 n.24 (1983).

F. The Role of Expert Opinion.

Proximate cause requirements cannot be dispensed with based simply upon an expert's assurance -- without empirically verifiable evidentiary support -- that the requisite factual connection exists between the act or event and the impact. Courts, for example, will not allow juries to rely on expert testimony unless it contains "a reasoned explanation illuminating why the *facts* have convinced the expert, and therefore should convince the jury, that it is more probable than not the [] act was a cause-in-fact of the plaintiffs injury." *Jennings v. Palomar Pomerado Health Systems, Inc.*, 114 Cal.App.4th 1108, 1118 (2003) ("[P]roffering an expert opinion that there is some theoretical possibility of the negligent act could have been a cause in fact of a particular injury is insufficient to establish causation." *Id.* (citations omitted; emphasis added.)

For example, an expert's opinion based on assumptions of fact without evidentiary support, or on speculative or conjectural factors, has no evidentiary value and may be excluded from evidence. *See, e.g., Pacific Gas & Electric Co. v. Zuckerman*, 189 Cal.App.3d 1113, 1135 (1987); *Lockheed Martin Corp. v. Superior Court*, 29 Cal.4th 1096, 1110–1111 (2003); *City of San Diego v. Sobke*, 65 Cal.App.4th 379, 396 (1998). Likewise, when an expert's opinion is conclusory because unaccompanied by a reasoned explanation connecting the factual predicates to the ultimate conclusion, "the opinion has no evidentiary value because an expert opinion is worth no more than the reasons upon which it rests." *Kelley v. Trunk*, 66 Cal.App.4th 519, 523–525 (1998). As a result, "an expert's opinion that something could be true if certain assumed facts are true, without any foundation for concluding those assumed facts exist . . . does not provide assistance to the jury because the jury is charged with determining what occurred in the case before it, not hypothetical possibilities." *Bushling v. Fremont Medical Center*, 117 Cal.App.4th 493, 510 (2004); *Jennings,* 114 Cal.App.4th at 1117-18 ("An expert who gives only a conclusory opinion does not assist the jury to determine what occurred, but instead supplants the jury by declaring what occurred.").

For these reasons, an expert opinion that there is a *theoretical* possibility that an act could have been a cause-in-fact of a particular event is insufficient to establish a legally cognizable showing of causation. *Saelzler v. Advanced Group 400*, 25 Cal.4th 763, 775–776 (2001); *accord, Leslie G. v. Perry & Associates,* 43 Cal.App.4th 472, 487 (1996). Instead, the plaintiff must offer an expert opinion that contains a reasoned explanation illuminating why the facts have convinced

the expert, and therefore should convince the jury, that it is more probable than not that the act was a cause-in-fact of the injury. *Jennings,* 114 Cal.App.4th at 1118.

Similarly, an expert may not rely on a model or methodology that cannot be empirically validated and is not reasonably established in the scientific or other expert literature. Evidence Code section 801 limits expert testimony to a matter "of a type that reasonably may be relied upon by an expert in forming an opinion upon the subject to which his testimony relates."[29] Courts of appeal have consistently recognized the duty to examine the basis for expert opinions and exclude testimony that lacks an empirical foundation and is not generally accepted in the scientific or expert community. *See, e.g., Pacific Gas & Electric v. Zuckerman,* 189 Cal. App. 3d 1113 (1987).

As with a court, an agency can and should disregard expert testimony that lacks an adequate factual foundation or is not based upon a generally accepted methodology. For example, "an expert's opinion which says nothing more than 'it is reasonable to assume' that something 'potentially ... may occur'" but has no basis in fact does not constitute substantial evidence that can reasonably be relied on by a public agency. *See Apartment Association of Greater Los Angeles v. City of Los Angeles*, 90 Cal.App.4th 1162, 1173-1176 (2001). *See also* Pub. Resources Code, § 21080(e)(2) ("Substantial evidence includes expert opinion *supported by fact* [and] not . . . unsubstantiated opinion or narrative.") (emphasis added).

[29] Similar rules prevail in federal court. Under the Federal Rules of Evidence, before an expert can testify to any "scientific, technical, or other specialized knowledge," a federal district court must be satisfied that "the testimony is based upon sufficient facts or data, the testimony is the product of reliable principles and methods, and the witness has applied the principles and methods reliably to the facts of the case." Fed. R. Evid. 702; *see also Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993).

V. APPLICATION

A compressed summary of the KMA nexus analysis is as follows:

1) Construction of New Market Rate Units

2) Determine Value of Market Rate Units
- Estimate sales price or rental rate of 5 "prototypical units"

3) New Household Occupies New Market Rate Unit
- All new households assumed to represent new income in Fremont

4) Estimate Income of Households
- For ownership households, assumes household spends 35% of income on housing costs; for rental households 30% of income spent on rent
- Uses Census data and makes adjustments to meet consistency with CA Health & Safety code standard

5) Estimate Income Available for Expenditures
- To adjust gross household income, assumptions are made about household, e.g.:
  -Federal and state income taxes
  -Contributions to social security and Medicare
  -Savings rates
  -Debt obligations

6) Estimate Expenditures of New Households
- Assumes 62% of gross income for large-lot single-family households and 67% for other ownership prototypes (which include expenditures on home purchase and rent)
- Assumes expenditures are in Alameda County

7) Use IMPLAN Model to Estimate Job Creation
- Assumes expenditures are in Alameda County
- Inputs net income available for household expenditures into IMPLAN model. (Assumes 62% of gross income available for expenditures for large-lot single-family households and 67% for other ownership prototypes
- Projects jobs generated at establishments that serve new residents directly; jobs generated by increased demand at firms which service or supply these establishments; and jobs generated when the new employees spend their wages in the local economy and generate additional jobs
- Jobs calculations are produced, including all jobs, full-time and part-time in Alameda County

8) Use IMPLAN Results to Calculate Jobs by Industry Category
- Calculations are based on IMPLAN output

9) Use of KMA Jobs Housing Model to Determine Compensation Levels
- Input number of jobs by industry in Alameda County into KMA model
- Sorts jobs by industry into jobs by occupation, based on national data, and attaches local wage distribution data to the occupations
- Quantifies compensation levels of new jobs

10) Estimate Employee Households Meeting Lower-Income Definitions
- Occupations translated to employee incomes based on County wage and salary info from EDD
- Model uses distribution of wages to calculate % of worker households in each income category
- For households with more than one worker, assumes individuals have similar incomes
- Step is repeated for each of the over 100 occupations and at each of the four affordable income tiers

11) Estimate Number of Households that Meet Size and Income Criteria
- Matrix is established to estimate the percentage of household income that would qualify in the affordable income tiers
- Output of the model is number of new worker households in Alameda County by income level "attributable to the new residential units and new households in Fremont."

12) Estimate Affordability Gap
- Match household of each income level with unit type and size according to governmental regulations and City practices and policies. For Very Low- and Extremely Low-Income, assume City will assist these households in multi-family rental units and that 4% low income housing tax credits paired with tax-exempt financing will be used as subsidy source.
- Estimate total development cost for affordable rental unit and ownership units (including profit) under normal market conditions
- Calculate maximum affordable purchase price and rental rate in each relevant income tier
- Output is "affordability gap:" the difference between cost of developing residential unit and the unit values at the affordable rents or sales prices.

13) Calculate Total "Nexus Costs"
- Calculate the total nexus cost per market-rate unit by multiplying affordability gap by number of affordable units for which demand is attributable to the market-rate unit Calculate per-square-foot nexus cost for each category of unit

At virtually every step, additional assumptions are made about factors such as household income, type, extent and location of expenditure of disposable income, multiplier effects, type and extent of new job generation, compensation, housing demand, size and income of new households, relationship to area median income, housing subsidies, commuting patterns and other variables.

As one economics modeling expert has observed, "since a given result can almost always be supported by a theoretical model, the existence of a theoretical model that leads to a given result in and of itself tells us nothing definitive about the real world."[30] It may help in understanding the implications of a particular set of assumptions (e.g., that expenditures in the local economy create jobs, which result in household formation and that new households create housing demand), but unless the assumptions are validated, the information is of little value.

> When we take a model "off of the bookshelf" and consider applying it to the real world, it is reasonable to ask whether it is based on assumptions that are generally in accord with what we know about the world and are capturing factors that are of first-order importance. In other words, we use the background knowledge that we have about the world we live in (knowledge that is based ultimately on empirical evidence) to filter out models that are not useful for understanding what happens in the economy or for making policy decisions.

In this case, in contrast to other development impacts for which fees or other mitigation measures are commonly imposed—such as traffic, sewer systems, schools, etc. -- there is nothing in the KMA study that constitutes any real-world evidence of many of its assumptions (e.g., that all new jobs lead to new households) or supports the cause-and-effect chain it postulates, such as specific examples of instances in which new market-rate construction has resulted in increased affordable housing demands. In the case of traditional development impacts, such as traffic and schools, both the assumptions and the effects have been empirically measured and validated. KMA's analysis, on the other hand, is a purely hypothetical construct – the result of modeling a carefully chosen set of assumptions that generate a specific result.

Nor, in contrast to more traditional development impacts, is there an intuitively obvious connection between new residential housing and the need for new affordable housing. In fact, both common sense and economic analysis support the opposite conclusion—that provision of

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[30] Pfleiderer, P., *Chameleons: The Misuse of Theoretical Models in Finance and Economics,* (Stanford, March 2014) at 2 (available at: https://www.gsb.stanford.edu/sites/default/files/research/documents/Chameleons%20-The%20Misuse%20of%20Theoretical%20Models%20032614.pdf)

new housing may alleviate the need for affordable housing as people move from older, less expensive homes to new homes. Several studies have shown that when a household moves into a new market-rate unit, a household with lower income typically purchases its existing house.[31] One such study tracked home sales in 13 cities and showed that each new home generated an average of 3.5 moves, all of which increased the available supply of existing homes.[32] The study reported that up to 14 percent of people who moved in the chain of upgrades generated by a new home were low-income, and 30% moderate income.

Additionally, if new market-rate housing was a significant factor in generating the need or demand for affordable housing, one would expect to find empirical support for this in the plethora of studies, reports, analyses and supporting data focusing on housing and the economic and demographic trends that play the most significant roles in generation of housing demand. Such analyses include, for example:[33]

(i) California Department of Housing and Community Development (HCD) analyses housing demand and the determination of regional housing needs; and reports and studies concerning the nature, extent and cause of affordable housing needs;[34]

(ii) Association of Bay Area Government (ABAG) regional housing needs determinations; employment forecasting and housing demand and demographic

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[31] Powell, B. and E. P. Stringham, *The Economics of Inclusionary Housing Reclaimed: How Effective Are Price Controls?* 33 Fla. St. U. L. Rev. 471, 496 (2005) (Economic studies show that as new homes are occupied, more housing becomes available at all income levels) (available at: http://www.law.fsu.edu/journals/lawreview/downloads/332/powell.pdf)

[32] Lansing, J., et al., *New Homes and Poor People* at 38-40 (Study of home sales in 13 cities showed that each new home generated average of 3.5 moves and that "any policy which increases the total supply of housing will be beneficial. The working of the market for housing is such that the poor will benefit from any actions which increase the supply in the total market.")

[33] The HCD, ABAG, Plan Bay Area and City of Fremont documents reviewed are listed in Attachment A and included in the attached CD.

[34] HCD -- Affordable Housing Cost Study (October 7, 2014); HCD -- Housing and Community Development 2014 Update, Highlights of the State Housing in California: Affordability Worsens, Supply Problems Remain (Nov. 2014); HCD -- Housing and Community Development May 19, 2000 Press Release regarding update of California Statewide Housing Plan.

projections. ABAG's population growth projections are used in regional planning efforts for issues such as affordable housing;[35]

(i) The studies and analyses conducted by ABAG, MTC and stakeholders in the development of Plan Bay Area, including forecasts of jobs, population, transportation and housing and the relationship between them; economic development and its impacts on employment, demographic and housing trends; and predictions regarding land-use patterns;[36] and

(ii) The City of Fremont's own planning documents, including the Housing Element of the General Plan.[37]

However, review of these studies, reports and planning documents shows no support for the KMA hypothesis -- none of these documents validates or even discusses the possibility of a cause-and-effect relationship between new market-rate housing and the need for affordable housing. Nowhere in these analyses are residential projects identified as having any potential impact on the need for additional housing – affordable or otherwise – or population growth.

The City of Fremont's 2015-2022 Housing Element, adopted on December 4, 2014, for example, references the need to provide housing for people working at redeveloped industrial and commercial facilities, but says nothing about any need for housing generated by new housing:

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[35] ABAG -- A Place to Call Home: Housing in the San Francisco Bay Area (2007); ABAG -- Regional Housing Needs Determination for the San Francisco Bay Area, 2001-2006 Housing Element Cycle (June 2001); ABAG Executive Board Nov. 2010 materials re Job, Housing, Demographic projections; ABAG Executive Board Nov. 2010 materials re Job, Housing, Demographic projections: Employment Forecasting Method & Determining 25 Year Regional Housing Need; ABAG Executive Board Nov. 2010 materials re Job, Housing, Demographic projections: 2014-22 Regional Housing Needs Determination and Allocation; ABAG -- Residential Demand and Development Potential in the San Francisco Bay Area Region, Working Paper 91-1 (Jan. 1991).

[36] Plan Bay Area -- Center for Continuing Study of The California Economy: A Review of the DOF and ABAG Population Projections to 2040; prepared for Association of Bay Area Governments (March 2013); Plan Bay Area – Final Forecast of Jobs, Population and Housing (ABAG/MTC July 2013); Plan Bay Area -- Overview of the Regional Housing Need Determination, DOF Population Projections and Plan Bay Area Forecast (2013); Plan Bay Area -- Regional Housing Need Plan for the San Francisco Bay Area: 2014-2022 (2013); Plan Bay Area: ABAG; Regional Policy Background Papers – Economic Development (July 2013); Plan Bay Area; Final Summary of Predicted Land Use Patterns (July 2013).

[37] City of Fremont, General Plan Housing Element (2007-2014); City of Fremont, General Plan Housing Element (2015-2022).

> The City's workforce is expected to grow by tens of thousands by 2035 as remaining vacant industrial lands are developed and older industrial and commercial sites are redeveloped, generating significant employment growth. Fremont needs housing for these workers, as well as for its teachers, its police and fire personnel, its nurses and child care workers and the retail and service workers that are the lifeblood of the local economy. Fremont also needs housing for seniors and others with limited mobility and fixed incomes.

Id. at 3.

Indeed, if anything, the City's housing element shows an *inverse* relationship between housing demand and job growth in the Fremont:

> Historically, the City was a bedroom community and had a jobs - housing ratio that was below the regional average. As Fremont matured, the number of jobs began increasing faster than the number of households. In 1990, there were 1.2 jobs per household in the City, compared to a regional average of 1.4. By 2000, the ratio had increased to 1.5 4 jobs per household in the City, which was on par with the regional average. *However, as the housing demands continued to increase, the total number of jobs did not keep pace, showing a decrease in jobs per household from 2000 to 2010 when the ratio decreased to approximately 1.26 jobs per household.*

Id. at 93. The Housing Element indicates that the "decrease reflects the downturn in the economy that occurred during that period," but notes that "[d]espite the decline during the recession, *ABAG expects the longer term trend to continue in the future*, with Fremont holding over 1.3 jobs per household in 2040." *Id.* (emphasis added).

Another place one would expect to see support for KMA's hypothesis is in CEQA analyses of the impact of residential development. Under CEQA, among other impacts routinely analyzed in environmental documents are those on population and housing. The Initial Study checklist requires evaluation of the potential impacts of projects on population growth, either direct or indirect, and this requirement is carried over into EIRs or negative declarations, requiring assessment of the potential impact of induced population growth. However, recent EIRs and negative declarations assessing the impact of new residential development in Fremont contain no mention of the impacts KMA postulates – creation of jobs through expenditures by residents of

market-rate homes that, in turn, create housing demand. This includes the EIR for the Warm Springs South Fremont Community Plan, which will include up to 4,000 new residential units. The EIR states:

> The Community Plan contemplates the development of up to 4,000 dwelling units within the plan area over the 22-year buildout horizon of the plan. Using the City of Fremont's average household size of 3.05, the Community Plan would be expected to add 12,200 residents to the City's population. However, the direct population growth that occurs pursuant to the Community Plan is considered "planned growth" because it has been contemplated by the City of Fremont General Plan. As such, development of housing within the Warm Springs/South Fremont Community Plan area would not be considered growth-inducing.

Id. at 7-4. There is no mention of any direct or indirect impacts from jobs generated by new residential development.

Notably, while the EIR projects that industrial, commercial and retail development under the Community Plan will create some 20,000 new jobs at buildout,[38] it concludes that the addition of these jobs would *not* result in any indirect population growth because there is "ample available labor:"

> Buildout of the Community Plan is projected to create as many as 20,000 new jobs over a 22-year period. This averages to 909 new jobs on an annual basis. For comparison purposes, the California Employment Development Department indicates that, as of October 2013, the City of Fremont had 5,600 unemployed persons, and Alameda County had 53,900 unemployed persons. *This serves to indicate that there is ample available local labor such that the Community Plan's new jobs would not result in indirect population growth.*

Id. at 3.8-9 (emphasis added)

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[38] "The proposed Community Plan identifies potential new development and redevelopment of properties to accommodate approximately 11,521,526 square feet of light industrial, research and development, office, retail, and hotel uses that would generate as many as 20,000 new jobs." *Id.* at ES-3.

Similarly, the EIR for the 2011 Fremont General Plan update concludes that, far from generating demands for new housing, the projected residential development would be *accommodating* of anticipated population growth:

> Implementation of the current General Plan would not induce population growth, since new residential development under the current General Plan would instead be intended to accommodate a portion of the City's share of the region's anticipated population growth, and would not involve the extension of infrastructure or public services to undeveloped areas to support new residential development.

Id. at 5-6.

Other recent EIRs and negative declarations for residential development projects in Fremont likewise contain no indication that the proposed development will result in generation of jobs that will fuel additional demand for housing.[39]

Moreover, the residential nexus study does not assess, rely on, attempt to controvert or even mention the substantial body of governmental and academic literature and supporting data identifying the structural causes of affordable housing needs. These data, studies and reports indicate that the lack of affordable housing is the result of a complex blend of factors, including restrictive zoning and growth controls, excessive impact fees, complex environmental regulations, multifamily housing restrictions, and NIMBYism. As set out in a comprehensive report prepared on behalf of HUD

> Regulatory mechanisms, such as restrictive zoning, excessive impact fees, growth controls, inefficient and outdated building and rehabilitation codes, multifamily housing restrictions, and excessive subdivision controls have been in use for decades. These controls have become more sophisticated and prevalent. The current regulatory framework makes building a range of housing types increasingly difficult, if not altogether impossible, in many areas. Although some recent market research appears to indicate a greater willingness by the general population to accept affordable housing for moderate or middle income families in their communities, no evidence exists that such abstract acceptance has

[39] *See, e.g.*, Dias Residential -- Draft Mitigated Negative Declaration and Mitigation Monitoring Plan; Niles Mixed Use Project (PLN2014-00338) -- Draft Mitigated Negative Declaration; Palmdale Estates (PLN2013-00189) -- Environmental Impact Report.

> translated into large-scale action at the local level to undertake significant regulatory reform.[40]

A consistent theme of these studies and reports is that affordable housing needs are a compound social problem that must be addressed through a comprehensive range of policy responses and measures (including streamlining the development approval process, eliminating restrictive zoning regulations, providing financial incentives, counteracting NIMBYism, reducing the complexity and uncertainty of environmental requirements). *Id.* at 10-13.

The City of Fremont's Housing Element acknowledges these realities:

> Even with appropriate General Plan land use designations and zoning in place, challenges remain in developing new housing, particularly affordable housing. As outlined in Chapter 5, the cost to develop housing, land costs, land use controls, and also neighborhood resistance to new development, including affordable housing are all factors inhibiting new housing development.[41]

The Housing Element is also frank about the role of NIMBY'ism in restricting development of affordable housing:

> Residents of established neighborhoods often resist new housing development, particularly affordable housing, out of concerns about increases in traffic, crime, school crowding, etc. This resistance to new development is often referred to as "NIMBYism" (Not in My Backyard-Ism). While NIMBYism is not the result of governmental action, the City can try to minimize it by providing opportunities for the public to learn about the benefits of affordable housing and the high quality of affordable housing developments.[42]

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[40] HUD -- "*Why Not In Our Community?" supra,* n.6 at 3.

[41] *Id.* at 23. *See also id.* at 151: "Regulations, while intentionally governing the quality of development in the Community, can also unintentionally increase the cost of development and thus the cost of housing. These governmental constraints can include land-use controls, local building and fire codes and their enforcement, on and off-site improvements, fees and other exactions required of developers as well as local processing and permit procedures."

[42] *Id.* at 172.

Unlike the above studies, reports and planning documents, which are based on empirical data, decades of professional experience, and a large body of existing literature, the residential nexus analysis makes no attempt to evaluate its assumptions empirically or to use the wealth of existing data on causes of affordable housing needs.

In addition to lacking any empirical justification and failing to controvert the large body of academic, technical and governmental literature identifying other causes of affordable housing needs, the residential nexus study employs a methodology that has not been generally accepted, or even considered, by the academic, scientific or technical community. A comprehensive review of potentially relevant sources in 2011 disclosed no literature -- peer-reviewed or otherwise -- supporting the methodology used in the residential nexus analyses.[43] It relies entirely on a combination of assumptions and modeling to construct a theory under which a market-rate home generates economic forces that create a "need" for a below-market-rate home.

But this analysis fails to demonstrate that the new housing has any *causative*, as opposed to correlative, relationship with the need for affordable housing. In contrast to traditional academic or scientific studies, in which other potential causes of a particular outcome are evaluated and eliminated (or otherwise accounted for), there is no attempt in the residential nexus study to evaluate data -- such as the historical correlation or lack thereof between development of market-rate housing and demand for affordable housing -- that would test the validity of the assumptions underlying the residential nexus study. Rather, the potential connection between new income in a community and affordable housing needs is evaluated in a purely abstract way, as if there were no other economic factors at play.

However, "[e]conomic phenomena play out in extremely complex, dynamic systems, in which outcomes are often determined by decisions made by millions of economic agents interacting in non-stationary environments."[44] Models can be useful in isolating and capturing important factors and connections,[45] but only if the conclusions of modeling are subjected to appropriate empirical validation:

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[43] Cray, A., *The Use of Residential Nexus Analysis in Support of California's Inclusionary Housing Ordinances: A Critical Evaluation: A report to the California Homebuilding foundation* (Nov. 2011) at 7 (available at http://www.cbia.org/go/linkservid/06D3172D-35C3-4C71-9A9098D439C63874/showMeta/0/).

[44] Pfleiderer, *supra*, n. 30 at 2.

[45] For example, a model used by ABAG -- UrbanSim -- describes how real estate development responds to demand. This Real Estate Development Model simulates the location, type, and density of real estate development, conversion, and redevelopment events at the level of specific

> Since a model can't include all economic factors (e.g., every possible market 'friction' and every possible incentive problem), the modeler needs to choose which factors are important. Results are determined not only by what is included *but also by what is excluded*.[46]

While the KMA analysis effectively isolates and examines the theoretical connection between new market-rate housing and affordable housing needs, it wholly fails to screen out other variables that could independently have caused the same outcome. Because the model does not even input and analyze the impacts of other factors, its utility even as a purely theoretical device is questionable. This, coupled with the failure to test its assumptions and conclusions against the real world, renders it essentially valueless as an aid to policy making. Without empirical validation, the assumptions plugged into the KMA models remain just that -- assumptions, ranging from the dubious (such as that every household contains people with similar incomes) to the untenable (such as that every new job within a city generates a new household in that city).

As Mayor Chuck Reed wrote to the San Jose City Council concerning a very similar KMA nexus analysis:

> The nexus study provided by our consultant does not prove that building market rate rental housing causes an increase in the need for affordable housing . . . . The nexus study is based on the assumption that proving causation is not necessary. In other areas, such as environmental impacts and transportation impacts, proving impacts is required before we can levy a fee . . . . Demonstrating a statistically significant correlation would allow us to strongly argue that there is a causal connection between building housing and the

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land parcels. The sub-model simulates the response of real estate developers to excess demand within land-use policy constraints. The algorithm examines a subset of parcels each forecast year and builds pro formas comparing development costs and income. New structures are built in locations where, all things considered, the development will yield a reasonable return. *See* Plan Bay Area; Final Summary of Predicted Land Use Patterns (July 2013) (available at http://planbayarea.org/pdf/final_supplemental_reports/FINAL_PBA_Predicted_Land_Use_Responses.pdf).

[46] *Id.*

> need for affordable housing. Without proof of causation, the housing impact fee "walks like a tax" and "it talks like a tax."[47]

Economic stimulus, new industrial and commercial development, the "multiplier" effect and other factors heavily influence both job creation and the demand for new housing—both market-rate and affordable. It is not possible to say with any degree of assurance that the residential development—as distinct from independent economic forces—causes any of the events or phenomena in the analytic chain, much less creates forces that, in continuous and active operation, lead to the need for affordable housing. Real estate development does not occur in the abstract -- it responds to demand generated by various market forces including demographic trends, economic growth, employment, housing supply and other factors, which influence demand both for housing at all income levels, not simply market-rate housing.[48]

Proximate cause minimally requires that "the probability that other forces alone produced the injury" be excluded. *Biron v. City of Redding*, 225 Cal. App. 4th 1264, 1279 (2014). "Causation turns on whether the act or event has "created a force or series of forces which are in continuous and active operation up to the time of the harm," and it is not enough simply to "create[] a situation harmless unless acted upon by other forces for which the actor is not responsible." Restatement (Second) of Torts § 433(b). Because there is nothing to indicate that the demand for affordable housing would not have existed without—and may well have preceded—the construction of the new housing, this most fundamental causal requirement is not satisfied.

Moreover, as discussed in detail above, proximate cause requires that the act or omission constitute a *substantial* cause-and-effect relationship . . . ." *Belair,* 47 Cal. 3d at 558–59. The Restatement explains that the word "substantial" is used to denote the fact that the party's conduct:

> has such an effect in producing the harm as to lead reasonable men to regard it as a cause, using that word in the popular sense, in which there always lurks the idea of responsibility rather than in the so-called "philosophic sense," which includes every one of the great number of events without which any happening would not

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[47] City of San Jose Memorandum from Mayor Chuck Reed Re: Housing Impact Fee (Nov. 17, 2014), available at http://www.sanjoseca.gov/ArchiveCenter/ViewFile/Item/2469; see also City of San Jose Memorandum from Councilmember Rose Herrera Re: Housing Impact Fee (Nov. 17, 2014), available at http://sanjoseca.gov/DocumentCenter/View/37588

[48] *See* Plan Bay Area; Final Summary of Predicted Land Use Patterns (July 2013) (http://planbayarea.org/pdf/final_supplemental_reports/FINAL_PBA_Predicted_Land_Use_Responses.pdf)

> have occurred. Each of these events is a cause in the so-called `philosophic sense,' yet the effect of many of them is so insignificant that no ordinary mind would think of them as causes.

Causal chains far less tenuous than this one have been rejected under proximate cause principles simply because there are too many assumptions piled upon assumptions. Here, the presence of so many steps in the analysis, any one of which can be heavily influenced in one direction or another by independent variables, renders the ultimate conclusion little more than speculation—the antithesis of the "substantial cause-and-effect" relationship required by law. *See Anza*, 547 U.S. 451 (no proximate cause when a court would have to engage in a "speculative" inquiry").

The length and complexity of the chain of causal reasoning, the number of variables that are highly sensitive to other factors, the failure to evaluate the impact of other potential causes and the absence of any empirical support for the analysis forecloses any argument that KMA nexus study proves that new residential development has a *substantial* cause-and-effect relationship with the need for affordable housing.

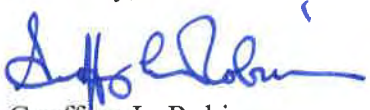
In addition to failing the first element of the proximate cause requirement—the substantial cause component—the theory of responsibility underlying the residential needs analyses fails the normative/evaluative component since it does not comport with the governing constitutional and statutory policies. The application of proximate cause to development mitigation necessarily embraces the policies of fairness and justice embodied in the state and federal constitutions, which preclude "forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." *United States v. Armstrong*, 364 U.S. 40, 49 (1960); *accord*, *Lockaway Storage v. County of Alameda*, 216 Cal. App. 4th 161, 183 (2013). If, for the reasons discussed above, it is not possible to say with any assurance that residential development is a substantial factor in creating the need for affordable housing, the "reasonable relationship" fundamental to development exactions is absent. The relationship between the development and the need is at best abstract and remote—the product of complex and largely theoretical studies commissioned solely for the express purpose of demonstrating a connection that many of the municipalities have expressly disavowed in their codes and ordinances.

It is also significant that the theory of responsibility underlying these studies has no coherent limiting principle. The low-income employees forecasted by the model may also be unable to afford many basic human needs other than new housing: health care facilities and services; transportation services and facilities; food and clothing; educational facilities and opportunities. Accepting the conclusion of the new generation of residential nexus studies—that local governments may impose on developers of new market-rate housing the responsibility to fund

the housing needs of these projected low-income employees—necessarily opens the door to requiring residential developers to fund these other needs. Such a result is neither fair nor just.[49]

The lack of affordable housing has been a critical issue in California for decades. As numerous studies have demonstrated, the paucity of affordable housing is the product of a highly complex interrelationship of economic, political and social factors, including local government resistance, fiscal disincentives, NIMBYism, CEQA, and lengthy permitting procedures. It will exist whether or not there is any new market-rate housing, almost surely in a more severe form in the absence of such development. It is a problem that, in fairness, should be addressed, and the costs borne, by society at large, not allocated to builders of market-rate housing based on studies that fail to satisfy the most basic elements of proximate cause.

Sincerely,



Geoffrey L. Robinson

Cc: City Manager
City Attorney
Community Development Director

Encls.

[49] Proponents of affordable housing exactions often argue that "housing is unique" because, they assert, unlike with other human needs, local governments have a constitutional obligation to provide adequate housing for all of their residents. This is untenable. California cities and counties are required by state law to zone sufficient sites at appropriate densities so that for-profit and non-profit developers have a realistic opportunity build the number of housing units identified in the local government's housing element. They are under no obligation to fund its development or ensure that it gets built. At all events, *Patterson* expressly rejected the argument that state housing law requirements—whatever their scope—allow cities and counties to impose exactions that do not satisfy basic nexus requirements.

ATTACHMENT A TO MARCH 2, 2015 LETTER
TO FREMONT CITY COUNCIL

ABAG -- A Place to Call Home: Housing in the San Francisco Bay Area (2007), available at http://www.abag.ca.gov/planning/housingneeds/pdf/resources/A_Place_to_Call_Home_2007.pdf

ABAG -- Regional Housing Needs Determination for the San Francisco Bay Area, 2001-2006 Housing Element Cycle (June 2001), available at http://www.abag.ca.gov/planning/housingneeds/pdf/RHND_Plan/RHND_Plan_2001-2006.pdf

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California City Finance -- Local Revenue Measures in California -- 2012 November Results (Feb. 2013), available at http://www.californiacityfinance.com/Votes1211final.pdf

California City Finance -- Local Revenue Measures in California -- 2013 November Results (Nov. 2013), available at http://www.californiacityfinance.com/Votes1311final.pdf

California City Finance -- Local Revenue Measures in California -- 2014 June Results (June 2014), available at http://californiacityfinance.com/Votes1406prelim.pdf

California City Finance -- Local Revenue Measures in California – 2014 November Results (Dec. 2014), available at http://www.californiacityfinance.com/Votes1411final.pdf

California City Finance -- Proposition 1A (2004) Facts (2007), available at http://www.californiacityfinance.com/Prop1A_FAQ.pdf

California Coalition for Rural Housing & Non-Profit Housing Association of Northern California, *Inclusionary Housing in California; 30 Years of Innovation* (2003), available at http://media.wix.com/ugd/8d7a46_f1a7892e03b249b7a0c391051b6c87b3.pdf

California Policy Center -- California vs. Texas in one chart, Housing Starts Authorized by Building Permits; 1 Unit Structures, 2011-2014 (May 2014), available at http://californiapolicycenter.org/california-vs-texas-in-one-chart/

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